The Development of Group Accounting in the United Kingdom to 1950

by

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A Thesis Submitted in Fulfillment of the Requirements for the Degree of Doctor of Philosophy of Cardiff University

Accounting & Finance Section of Cardiff Business School, Cardiff University

April 2009

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Abstract

This thesis is on the development of group accounting in the United Kingdom in the first half of the twentieth century. Group accounts are normally thought identical to consolidated accounts, but the term 'group accounts' is a wider term than 'consolidated accounts'. There is an important preceding research (Edwards and Webb, 1984) that revealed a wide range of group reporting procedures experimented by British holding companies during the 1920s.

In this thesis, an attempt is made to develop a theory-based explanation to the following question: 'Why was the adoption of consolidated accounts slow in the UK?' The study selects two units of analysis, (1) British holding company directors' group accounting practices and (2) the British accountancy profession's attitude towards group accounting. For the former unit, a much larger data set was selected than the previous literature in order to provide further and more conclusive evidence.

The findings reveal the initial adoption of the equity basis of group accounting by company directors, and provide a plausible explanation based on a comprehensive study of the pre-1930 literature on group accounting. This study also discovers that the prominent professional accounting journal, *The Accountant*, was a consistent advocate of group accounts, but that contributors to its columns failed to agree upon consolidated accounts to be the 'right' method of group accounting. New evidence to show that the ICAEW's decision to provide strong support for consolidated accounts might be attributed to F.R.M. de Paula's late intervention in the regulatory formulation process is also presented.

Applying the theory of path dependence, this study concludes that the preference for legal entity-based accounts, which was influenced by the accountancy profession's attitudes towards group accounting, was shared by a large number of British holding company directors and became slow to change.

Acknowledgements

This study is deeply indebted to the invaluable guidance and assistance from my doctoral supervisors, Professor John Richard Edwards, Professor Trevor Boyns and Professor Howard Mellett.

I wish to express my sincere gratitude and largest appreciation to my chief supervisor, Professor Dick Edwards. Without his unfailing support and care, I could never have hoped to complete this study. Throughout my doctoral course, he maintained a deep patience, and his professional comments and supportive suggestions, combined with the warm encouragement, continuously improved my poor drafting. I wish to express my loyalty and respect for him as a professional accounting historian and as a human being.

I have enormously benefited from the sound and constructive comments and suggestions from Professor Trevor Boyns. He has been taking a heavy responsibility as the Director of Postgraduate Research Studies Programme at CARBS, but he has generously retained his efforts to assist my thesis and, whenever he gave me back my draft of thesis, it was filled with red handwritten annotations. His clear statements in the complex and conceptual discussion have always paved the way for a better drafting.

I am further obliged to the insightful advices from Professor Howard Mellett. His responses were prompt, and his suggestions were constructive. He provided crucial comments and advice on my drafts in order to improve the quality.

I would like to gratefully acknowledge the support of the Guildhall Library in London, the Institute of Chartered Accountants in England and Wales in Milton Keynes, which generously gave me permission to access their archival sources. The staffs of all these organizations have been extremely helpful in discovering the materials.

Thanks are also due to Ritsumeikan University, Japan, for sponsoring my research in Cardiff and enabling me to progress to this further stage in my academic life, and to the ORS Awards Scheme of the United Kingdom for providing me with financial assistance.

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Chapter 1 Introduction

1.1 Background of the study

Accounting history is a topic which has been vigorously discussed among academics, especially since the term 'new accounting history' was introduced in 1991 (Miller, Hopper and Laughlin, 1991). Carmona and Zan (2002: 291) believe that 'Research in accounting history witnessed a golden age during the 1990s'. Walker (2006: 107) also states that 'The last few years have witnessed a number of significant developments in accounting history research'.

Today, the number of published papers on the subject has so grown[1] that two compendia of accounting history articles, representative of the growth and diversity of accounting history research, were compiled and published in 2000 and 2006 (Edwards ed., 2000; Fleischman ed., 2006). Most of the articles in these compendia were published during and after 1990s (Figure 1-1). Edwards selected nine papers published in each of 1995 and in 1996, eight papers published in 1990, and seven papers published in 1993. Fleischman also reprinted five papers from 1991 and 1999, four papers from 1994, 1996 and 1998, and three papers from each of 1992, 1993, 1997 and 2004. Accordingly, it seems plausible to say that accounting history is a 'hot topic' among today's academic researchers.

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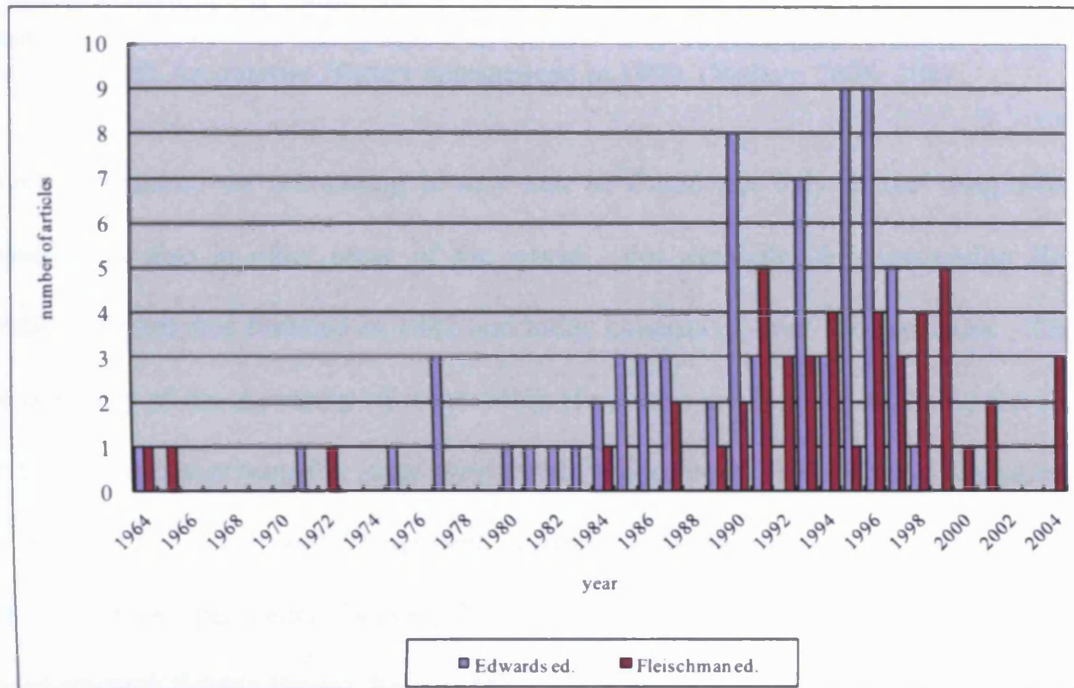
[1] For helpful bibliographies of accounting history publications, see Anderson (2002a, 2002b, 2003, 2004, 2005) in *Accounting, Business & Financial History*, and Foreman (2001, 2002, 2003, 2004, 2005) in *Accounting History*. For an analysis of historical publications appearing in particular journals, see, for example, Napier (2006) on the first 30 years of *Accounting, Organizations and Society*.

Figure 1-1 The number of articles appearing in the two compendia of accounting history



Source: Edwards ed., 2000; Fleischman ed., 2006

Of course, it can be noted that 'U.S.-based, flagship journals, the *Accounting Review* and the *Journal of Accounting Research*, formerly served as outlets for historical offerings, but now will not even send history articles out for review' (Fleischman, ed., 2006: xviii). The situation today presents a sharp contrast to that in 1970s when R.H. Parker (1977a: 1-2) observed that 'The *Accounting Review* has continued to give generous space to the subject [of accounting history]'.

Nevertheless, as can be seen in Figure 1-1, accounting history is a fairly flourishing discipline world-wide today. Walker (2006: 108) describes the 'joyful years' as follows:

> *Accounting, Business & Financial History* (1990) and *Accounting History* (New Series, 1996) joined *The Accounting Historians Journal* (1974) as specialist journals in the field. There were special issues on accounting history in mainstream accounting journals and a significant volume of history papers in esteemed outlets such as *Abacus*; *Accounting, Organizations and Society*; *Accounting, Auditing & Accountability Journal* and *Critical Perspectives on Accounting* ...

> Perhaps as significant a feature of the 1990s was the fact that, increasingly, accounting historians were accepted as having a legitimate presence in the modern business school ... In addition to the World Congress of Accounting Historians in the US, an annual conference at Cardiff Business School (later aligned to *Accounting, Business & Financial History*) was inaugurated in 1989. An international biennial conference associated with *Accounting History* commenced in 1999. (Walker, 2006: 108)

The lively discussion on accounting history can be found not only in the 'Anglo-Saxon' community, but also in other areas of the world. For example, the Accounting History Association (Japan) was founded in 1982 and today consists of over 200 members. Six per cent of members of the Academy of Accounting Historians are from Japan, being the second largest body and comprising the same proportion (six per cent) as the United Kingdom (the United States is the largest with 71 per cent, Australia is fourth with four per cent and Canada is fifth with three per cent) (Walker, 2006: 115). Accounting history is also a lively discussed research field in France, Italy and Spain.

> Annual conferences on accounting and management history were inaugurated in France and the European Institute for Advanced Studies in Management (EIASM) convened periodic workshops on the history of accounting and management practice. (Walker, 2006: 108)

> The Societa Italiana di Storia Della Ragioneria (SISR) (*Italian Society of Accounting History*) traces its origins to 1984 and boasts over 200 members. ... The first volume of its journal, the biannual *Contabilita e Cultura Aziendale*, appeared in 2001. In December 2004, the first issue of *De Computis: Revista Espanola de Historia de la Contabilidad* (Spanish Journal of Accounting History) was published. (Walker, 2006: 117)

Why has accounting research blossomed only in the relatively recent past? There are numerous reasons which include the fact that in some countries (e.g. Britain) accountancy has only flourished as a university subject in the last thirty years or so, and the fact that it is only in recent decades that scholarly and provocative articles on accounting history have helped to stimulate study (Edwards, ed., 2000). But the position is now quite different, and part of the reason may be increased recognition of the many purposes that the study of accounting history serves: 'historical research in accountancy offers useful insights into present and

possible future issues, supplementing the "positive" (is) and the "normative" (ought) with the "historical" (was)' (Previts, Parker & Coffman, 1990b: 151). According to a sometime president of the American Institute of Certified Public Accountants, studying historically is simply a natural activity for some of accounting researchers[2]. Peloubet (1955: 9) stated as follows:

> The study of the historical background of the profession is much more than a mere exercise in antiquarian research. We cannot understand our present position fully without having some idea of how we got there. The background of the development of an accounting method or principle is often quite important in determining its scope or application. (Peloubet, 1955: 9)

In an overview of the reasons for studying accounting history, Edwards (1989a: 3-6) provides four convincing reasons[3]. First, it is '*recreational*', in other words, 'pure enjoyment is a quite sufficient reason for studying accounting history' (Edwards, 1989a: 3). Second, it is '*intellectual*', because 'the study of accounting history helps us to understand our past and gives us an appreciation of how our current practices and problems came into being' (Edwards, 1989a: 4). Third, it is '*problem solving*', as 'some argue that the study of accounting history provides insights for the solution of present-day accounting problems and helps predict future likely developments' (Edwards, 1989a: 5). In Edwards' opinion (1989a: 5), 'these are ambitious claims which must be treated with some caution, but we can probably agree that the subject has some contemporary relevance'. Fourth, accounting history might serve as a basis for 'making predictions', with an example of this contribution being Mumford's study of 'A Familiar Inflation Accounting Cycle'. This 'drew close parallels between events in 1948-54 and 1973-78, and led [Mumford] to the correct conclusion that interest in reform would dwindle with the rate of inflation' (Edwards, 1989a: 6). It is

[2] The literature on accounting history nevertheless has a long tradition: 'published accounting history works such as Worthington's (1895) date from the late 1800s' (Previts, Parker & Coffman, 1990a: 1).

[3] Napier (1989) also provides a good justification for accounting history as a legitimate subject for study. He presents three 'conceptual frameworks' (understanding the past, contextualising accounting, and the new positivism) that have motivated accounting history researchers.

considered in this study that the above four reasons are sufficient to explain why, increasingly, an historical approach is employed for accounting studies.

1.2 The aim and context of the study

The aim of this thesis is to obtain an understanding of the development of group accounting in the United Kingdom (UK) in the first half of the twentieth century. Today, the terms group accounts and consolidated accounts are used interchangeably, but 'technically speaking they are not exactly the same' (Brennan, 2005: 129), and this is abundantly evident when studying historical developments. In this study, the term 'group accounts' is used as 'all forms, whether consolidated or otherwise, of accounting statements which show the position and earnings of the group from the standpoint of the shareholders in the holding company' (Robson, 1956: 7). Therefore, the word 'group accounts' is a wider term than 'consolidated accounts'. In the UK context, it is important to pay attention to this difference of terminology, because of the fact that 'a wide range of methods of accounting for the results of subsidiary companies was in use by the early 1930s, and the number of companies employing group reporting procedures were clearly not insignificant' (Edwards and Webb, 1984: 41). This thesis takes into consideration not only consolidated accounts but other forms of group accounting for the purpose of obtaining a better understanding of the developmental process. However, for reasons explained in chapter 2, the principal focus will be on the following two methods of group accounting, namely the equity method[4] and consolidated accounting.

[4] In this study, 'the equity method' means the inclusion of a proportional share of the profits and losses of subsidiary companies in the holding company's statutory (legal entity-based) accounts irrespective of dividends actually declared or paid. This method enables the holding company's accounts to show the consolidated amount of profit or loss of the holding company and its subsidiary companies, by taking credit for a share of profits (losses) of subsidiary companies and carrying the investment at cost plus the share of undistributed profits (Parker, 1984: 69). Therefore, on the one hand, it is a modification of legal entity-based accounts, but on the other hand, it can be characterised as a group accounting method. The equity method today is applied to consolidated accounts in order to incorporate the results of associated

In the UK, at the beginning of the twentieth century, financial reporting requirements were introduced for companies registered under the Companies Act. The Companies Act of 1900 imposed an obligation on directors to present to shareholders an audited balance sheet which, from 1907, had also to be filed with the Registrar of Companies and be made available for public scrutiny (Edwards, 1989a: 128). It seems to be the case that, as far as the strict legal position was concerned, 'there existed no general legal requirement that the balance sheet presented to shareholders should be confined to the strict legal entity' (Edwards and Webb, 1984: 45), since the provision stated that 'A balance sheet shall be made out in every year and laid before the company in general meeting made up to a date not more than six months before such meeting' (Companies Act 1908, First Schedule, Table A, Section 107). However, Edwards and Webb (1984: 45) discovered that the obligation to present the legal entity-based balance sheet to shareholders attending the annual general meeting was usually implied by the company's relevant article of association modelled on that recommended for adoption by Table A in the First Schedule to Companies Act 1908 (Companies Act 1908, Section 10). They recorded that Pearson and Knowles' article 152 required the balance sheet to set out the 'property and liabilities of *the company*' (*emphasis added*)[5].

By about fifty years later, in addition to the 'legal' balance sheet, the publication of 'group accounts' had become required by statutory provisions. The Companies Act 1948 (hereafter, CA48) defined group accounts as 'accounts or statements dealing ... with the state of affairs and profit or loss *of the company and the subsidiaries*' (*emphasis added*) (CA48, Section 150), and it required them to be laid before the company in general meeting. The group accounts so required were normally expected to be in the form of consolidated accounts

---

companies and joint-ventures. However, as Nobes (2002: 18) stated, 'in the U.K., the earliest use of the equity method appears to be for the purpose of including subsidiaries in the financial statements of investors as an alternative to consolidation'. See section 4.4 of chapter 4 for the definitions of this and other group accounting methods studied in this thesis.

[5] In addition, Edwards and Webb (1984: 45) noted that 'as regards the filing requirement, it does seem that CA 1908, Section 26(3), implied a legal obligation for directors to deliver a legal entity based balance sheet to the Registrar, then located at Somerset House'.

(what would today be described as the 'benchmark' treatment), comprising (a) a consolidated balance sheet and (b) a consolidated profit and loss account (CA48, Section 151(1)). However, other forms were permissible if, in the opinion of the directors, a better presentation of the same or equivalent information could be achieved that could readily be appreciated by shareholders. In particular, the group accounts might consist of (1) more than one set of consolidated accounts dealing with other groups of subsidiaries, or (2) separate accounts dealing with each of the subsidiaries, or (3) statements expanding the information about the subsidiaries in the company's own accounts, or (4) any combination of those forms (CA48, Section 151(2)). Moreover, it was permitted that the group accounts might be wholly or partly incorporated in the company's own balance sheet and profit and loss account (CA48, Section 151(3)).

There was, accordingly, a major accounting change concerning group accounting regulations in the UK in the first half of twentieth century. This was accompanied by major movement in accounting practice. The 'legal' accounts were the only accounts that companies prepared and presented at annual general meetings at the beginning of the twentieth century. By the end of the period examined (1950), consolidated accounts came to be published in addition to the legal entity-based accounts. This study aims at obtaining a better understanding of the change process.

There have been a number of prior studies designed to trace the developmental process of group accounting in the UK (Edwards and Webb, 1984; Kitchen, 1972; Parker, 1977b; Walker, 1978; Wilkins, 1975), the United States (Childs, 1949; Moonitz, 1951; Walker, 1978), Australia (Walker, 1970; Whittred, 1986, 1988; Walker and Mack, 1998), Spain (Mora and Rees, 1988), and Japan (Kawamoto, 2001). Moreover, the British experience in contrast to the American experience has been paid significant attention in a sequence of prominent studies (Bircher, 1988; Edwards, 1991; Edwards and Webb, 1984; Hein, 1978; Kitchen, 1972;

Parker, 1977b; Walker, 1978). The following are the main features of the developmental process in the UK as expressed in the previous literature. First, Gilbert Garnsey (a partner in the leading firm of Price, Waterhouse & Co.) vigorously expressed his view in 1922 that consolidated accounts were valuable, and this intervention played an important role in the development of group accounting theory and practice in the 1920s (Kitchen, 1972). During the 1920s and early 1930s, companies experimented with a wide range of group reporting procedures, including consolidated accounts (Edwards and Webb, 1984). The report by the Greene Committee and the Companies Act of 1929 (hereafter, CA29) did not introduce consolidated accounts as a legal requirement, although the subject was widely and carefully discussed (Bircher, 1988; Edwards, 1989a; Kitchen, 1972). The Royal Mail case of 1931 and the 'trail blazing' accounts published by the Dunlop Rubber Co. in 1933 stimulated some companies to publish consolidated accounts (Edwards, 1989a; Kitchen, 1972; Walker, 1978). In spite of the Royal Mail case and publication of Dunlop's consolidated accounts, there was limited use of consolidated accounting in practice prior to 1945 (Bircher, 1988; Arnold and Matthews, 2002). F.R.M de Paula was an influential figure on the emergence of Recommendation on Accounting Principle VII (hereafter, RoAP7), issued by the ICAEW in 1944, which provided formal encouragement for all holding companies to publish group accounts, normally in the form of consolidated statements (Kitchen and Parker, 1994; Zeff, 1972).

Table 1-1 is a fuller list of historical events in the development of group accounting in the UK, up to 1950, revealed by the previous studies.

Table 1-1 Historical events in the development of group accounting in the UK

Year	*Events*
1910	The earliest British example of a consolidated statement, known so far, was published by the directors of the Pearson & Knowles Coal and Iron Co. Ltd.
1922	A statement displaying a summary of the group's assets and liabilities was published by Nobel Industries.
1922	Sir Gilbert Garnsey presented a paper entitled 'Holding Companies and their Published Accounts' to the London members of the ICAEW, which later was published in *The Accountant* and in book form.
1929	CA29 required holding companies to state how the profits and losses of subsidiaries had been dealt with in the accounts of the holding company.
1931	The Royal Mail case revealed that under the regulations of CA29 it was possible for directors of holding companies to inflate reported profits by making inter-company transfers of dividends.
1933	The 'trail blazing' accounts were published by the Dunlop Rubber Co. in consolidated form.
1939	The London Stock Exchange required directors of holding companies, seeking a quotation, to undertake to issue shareholders with a consolidated balance sheet and profit and loss account.
1944	RoAP7, issued by the Institute of Chartered Accountants in England and Wales, provided formal encouragement for all holding companies to publish group accounts, normally in the form of consolidated statements.
1948	CA48 required holding companies to lay group accounts, normally in the form of consolidated statements.

Sources: Edwards (1989a), *The Accountant*.

One reason for the wealth of prior literature on the subject seems to be the fact that, as noted above, British holding company directors' publication of group accounts in addition to the legal entity-based accounts exhibits an important case of accounting change. It has been considered by academic researchers on accounting history that the process of change in accounting is a topic of both interest and importance, but it remains a neglected area requiring further research (Edwards, 1991; Hopwood, 1987). For example, Hopwood (1987: 207) addressed it as follows:

> Accounting is not a static phenomenon. Over time, it repeatedly has changed. New techniques have been incorporated into the accounting craft. It has been called upon to serve an ever greater variety of different and changing purposes. ...
>
> When seen in such terms, accounting continually has had a tendency to become what it was not. A fluid and emergent craft, its techniques and their attendant perspectives have been implicated in a number of very different ways in organisational and social transformations. Unfortunately, however, very little is known of the processes of accounting change. (Hopwood, 1987: 207)

A study of the accounting practices of holding companies (from a single set of legal entity-based accounts to the simultaneous publication of group accounts in addition to legal entity-based accounts) exemplifies an important arena of accounting change. It is intended that this thesis will extend and deepen the study and understanding of this process.

Another reason why a number of accounting historians have worked on the subject reflects recognition of the fact that the development of group accounting varies across countries. For example, Parker (1977b: 203) noted that 'accounting theory and practice in relation to consolidated accounts still differ considerably from country to country, even in such advanced industrial nations as the US, the UK, the Netherlands, the German Federal Republic and France'. The difference between the experience of the UK and that of the United States (US) has attracted particular attention to date. As Kitchen (1972: 114) stated, 'at the beginning of the 1920s, the holding company group was still a relatively new phenomenon in this country, though it was already well established in North America'. Peloubet (1955: 31) observed the same situation, further stating that 'the British accountants lean much more to the adjustment and amplification of the holding company statements than do their colleagues in the United States'. Walker (1978b: 100) also pointed to the difference that resulted from the fact that 'North American and British accountants developed differing rationales for the presentation of consolidated statements'.

Certainly, there has been paid particular attention to the difference in timing of holding company directors' adoption of consolidated accounts in the US and in the UK.

American directors introduced consolidated accounts before British directors adopted them. For example, in the US a number of consolidated financial statements were published well before 1900[6] and consolidation accounting became the required method for income tax returns by the Revenue Act of 1918 (Hein, 1978: 273). On the other hand, in the UK, the first known example of consolidated accounts prepared by a British company[7] is that of the Pearson and Knowles Coal and Iron Co. Ltd in 1910 (Edwards, 1991), and even the CA29 did not require holding companies to publish group accounts. Accounting historians have thought that British accountancy made slow progress compared to its American counterpart concerning the development of group accounting (Edwards, 1989a: 230; Hein, 1978: 283; Parker, 1977: 206).

A study of the difference described above is important and might be paid particular attention today when international harmonization of accounting is widely and vigorously discussed. For example, Nobes and Parker stated as follows:

> The harmonization reason has grown steadily in importance in recent years ... [however] major problems such as lease accounting, *consolidation accounting* ... have been tackled in different countries in significantly different ways. (Nobes and Parker, 2004: 8-9) (*emphasis added*)

Thus, it can be said that studying the development of group accounting in the UK has been, and still is, an important subject of accounting history for the above two reasons. This thesis is in this connection intended to make a contribution to the body of accounting historiography.

[6] For example of industrial company, the National Lead Company published consolidated statements in 1892 and it was followed by the General Electric Company in 1894 (Childs, 1949:44).

[7] For a municipal corporation, Coombs and Edwards (1995: 97) present an actual example of an aggregate balance sheet (Bradford's account for 1900) which brought together the year-end balances for each of the funds and departments.

1.3 Research question and methodology

1.3.1 Research question

As mentioned in the previous section, the development of group accounting in Britain has been paid particular attention on the grounds that 'it has failed to introduce improved procedures when the need for change was clear and obvious' (Edwards, 1989a: 15)[8]. However, despite the fact that a number of researchers have worked on the subject, there are key questions that remain unresolved. The questions are:

- 'Why did it take so long for the publication of consolidated group statements to become established practice in Britain? In particular, why, after an initial measure of acceptance, did it encounter so much opposition in 1925[9]?' (Kitchen, 1972: 134-5)
- 'Why specific companies failed to provide group accounts throughout the 1930s and into the 1940s?' (Bircher, 1991: 295-6)

Kitchen's paper (1972) was based on an examination of Garnsey's lecture on 'Holding Companies and their Published Accounts' delivered to the London Members of the ICAEW in December 1922, the relevant content of leading journals and magazines, publishing professional and business opinion on the matter at that time, such as *The Economist*, *The Times* and *The Accountant*, and evidence submitted before the Company Law Amendment Committee (Greene Committee) in 1925. The paper was a pioneering work on the subject and it became the foundation for later research on the topic. But despite the thorough investigation that he undertook, Kitchen (1972: 134-5), when concluding his paper, still asked himself the above question.

Bircher (1991) is a book on change in the law and practice of accounting from 1929 to 1948. A study of the development of consolidated accounts appears as chapter six of the

[8] This notion of 'slow progress' is not only held by accounting historians today but also conceived by accountants of the day. For example, it was claimed that 'in one particular the accounts published by American companies are *much in advance* of those published in Great Britain, and that is in the case of holding companies so called, *i.e.* those which hold all the shares in a large number of operating companies' (Dickinson, 1924: 272) (*emphasis added*).

[9] 1925 is the year when Greene Committee (Company Law Amendment Committee chaired by Wilfred Greene) was arguing the possibility of legal requirements for consolidated accounts.

book and was also published as Bircher (1988). Bircher (1988) is an examination of actual published accounts of the 40 largest holding companies, by market capitalisation, extracted from the rankings of the largest manufacturing companies in 1930.

Kitchen (1972) and Bircher (1991) were therefore in-depth investigations of the development of group accounting in the UK, but they still needed to ask themselves the above questions when they had concluded their works, and these issues remain unresolved today. It is therefore the purpose of this thesis to obtain a better understanding of the nature of the developmental process towards group accounting.

The questions raised by Kitchen (1972) and Bircher (1991) can be said to ask substantially the same thing. It is of course true that Bircher uses the term 'group accounts' rather than consolidated accounts as used by Kitchen, but Bircher's question was based on his finding of 'the absence of any very significant rate of adoption of *consolidated accounting practices* by companies in the sample even as late as 1945' (Bircher, 1988: 10, *emphasis added*). Also, the title of Bircher's paper was 'The adoption of consolidated accounting in Great Britain' (Bircher, 1988). Therefore, it is reasonable to assume that the research questions are both related to consolidated accounts, only, rather than dealing with group accounting more widely. Thus, the two questions can be rephrased as one research question that this thesis will address.

Why was the adoption of consolidated accounts slow in the UK?

1.3.2 Units of analysis

There are two units of analysis for this study, following the previous literature. As addressed above, Kitchen (1972) paid attention to 'professional and business opinion'; in other words to the views of business men and the accountancy profession. Similarly, Bircher (1988) contrasted principle and practice, saying that 'although the principle of consolidated

accounting had gained widespread approval it is not clear to what extent this was reflected in the accounting practices adopted by holding companies' (Bircher, 1988: 4). In this study, British holding company directors' group accounting practices and the British accountancy profession's attitude towards group accounting will be selected as units of analysis.

The first unit of analysis, 'business opinion' will be derived from an investigation of group accounts that British holding company directors actually published. In order to obtain a collective opinion of British business men at that time, this study does not specify any individual company. Instead, it examines 1,545 sets of accounts published by British holding companies, selected from a dataset of 2,943. This approach (reported in chapters 4 and 5) prevents the study from undertaking a detailed investigation of each case but, in the endeavour to provide a possible answer to the above research question, this thesis follows the previous literature of studying business opinion as a whole.

The second unit of 'professional opinion' will be obtained from three different sources of materials in this study. It will be represented by the views of leading accountants and contemporary writers in chapter 6, the content of *The Accountant* in chapter 7 and the conclusions reached by the ICAEW's leadership in chapter 8. The reason for the choice will be further explained in each chapter. Thus, it must be noted here that, when discussing attitudes towards group accounting, the word 'profession' is used in this study to signal the views of professional accountants rather than those of specific professional bodies.

1.3.3 Conceptual framework

It must be stated clearly here that, although this study introduced as the research question 'Why was the adoption of consolidated accounts slow in the UK?', some previous literature did try to provide possible answers to the issue. A detailed survey of the answers will be presented in 2.2.2.3 of chapter 2, but it is enough to say here that there has been presented

more than six reasons for the slow adoption of consolidated accounts in the UK. The contention of this thesis, however, is that the six reasons are not considered a full explanation. It has been indicated in the prior literature (for example, see Edwards and Webb, 1984: 41) that there might be more reasons for slow change. However, this study does not seek to discover a further contributing factor. Instead, it will seek to uncover a more fundamental, holistic, explanation for the slow development of group accounting in the UK.

In order to develop a more fundamental explanation for the slow adoption of consolidated accounts in the UK, it is considered helpful to employ, if possible, a conceptual theory, because it is not always easy to relate cause and effect successfully based solely on available archival evidence. For the purpose of this study, this thesis will employ the idea of path dependence, developed in the evolutionary economics literature, and draw upon insights provided by the old institutional economics based accounting studies that themselves rely on that framework. Path dependence is chosen in this thesis because both the research question of this study and the concept of path dependence are equally concerned with the slowness of changing process. The research question refers to the slow adoption of consolidated accounts in the UK, and path dependence implies a stable situation where human agents tend to make minimum changes to their action because what they do is not only a result of their personal decision but also a reflection of the shared expectation of many other people surrounding the agent.

The idea of path dependence has been widely used and discussed in different ways in different academic fields. For this study, a central concept is that 'history matters', and, in the context of the evolutionary theory of economics, history matters because 'habits' are an important feature of human behaviour. As explained more fully in chapter 3, habits are repeated behaviour of individual agents, but over time such behaviour can be institutionalised when shared by a group of agents. According to the framework provided by the old

institutional economics based accounting studies, the institutionalised behaviour is slow to change, taking much time to be altered. This study considers that the idea of path dependence has potential to explain the slow adoption of consolidated accounts in the UK in a persuasive manner[10].

1.4 Structure of the thesis

In chapter 2, the empirical literature and theoretical literature which are of relevance to this study will be surveyed. It will be shown that there have accumulated a number of prior research studies which specifically focused on group accounting, but that there still remains much to study. Attention will be drawn to the 'research question' that is central to this study, and it will be argued that a more persuasive and fundamental explanation for the development of group accounting in Britain is required. It will also be argued that much recent research into accounting history has been involved with methodological issues and that the 'recent Neoclassicism' seems to be the most appropriate framework for the purpose of this study. Chapter 3 explains further the methodology employed in this study and introduces the concept of path dependence to help explain the slow adoption of consolidated accounts in the UK. The concept of path dependence is considered to be a result of 'habits', which over time will be institutionalised and will gain resistance to change.

Chapters 4 and 5 deal with British holding companies' group accounting practices from 1927 to 1951, the former presenting the findings from original empirical data and the

[10] It will be explained in section 3.2 of chapter 3 that the concept of path dependence was chosen rather than other theoretical paradigms because it focuses on 'stability'. This thesis sees two contrary dimensions to the development of group accounting in the UK. One dimension is the changing process that encouraged British companies to adopt consolidated accounts, and the other is the stabilising factors that discouraged change. The research question of this study is concerned with the latter process, i.e. stability of accounting, which is a notion thought to be consistent with the idea of path dependence. The different meaning attached to two apparently similar words – 'stability' and 'continuity' – by accounting history literature will be explained in the footnote 28 in chapter 3.

latter analysing and interpreting those findings. Three main findings will be presented. (1) The number and proportion of quoted companies adopting group accounting procedures grew during the period from 1927 to 1951. (2) The rate of adoption of consolidated accounts increased particularly in the periods of 1946/47 and 1950/51, which was after RoAP7 and CA48 respectively took effect. (3) The equity method was used by a fairly constant percentage of holding companies from 1930/31 onwards. An analysis using four variables relating to the companies investigated (their auditors, their size, the stock exchange on which they were quoted and their type of business) will be conducted in the endeavour to explain the findings (1) - (3).

Chapters 6-8 address the accountancy profession's attitudes towards group accounting. As noted above, depending on the availability of evidence and the importance of the evidence, in the context of the issue discussed, the definition of what is considered to constitute the opinion of the accountancy profession will be different in each chapter. It will be shown that the equity method was favoured by the early literature (chapter 6) and this is considered to be an explanation for the initial adoption of the equity method by British holding company directors. In chapter 7, it will be discovered that, although consolidated accounts were paid particular attention, writings published in *The Accountant* did not reach a firm decision, until the issue of RoAP7, concerning which of the available group accounting practices was the 'best' method to adopt. This finding of absence of agreed method of group accounting will be considered to be a possible excuse for holding company directors to publish no group accounts. It will be also seen that de Paula's strong influence on the creation of RoAP7 can be confirmed whereas, during the 1940s, other accountants among the ICAEW leadership remained unwilling to decide whether or not consolidated accounts were the 'best' method of group accounting (chapter 8).

Chapter 9 provides a conclusion that attempts to answer the thesis's research question

based upon the conceptual framework and acknowledges issues that this study did not deal with but require further research. It will be concluded that, in the history of group accounting in the UK during the first half of twentieth century, British holding company directors' adherence to legal entity-based accounts can be partly attributed to the writings of prominent accountants during the 1920s and the lack of consistent advice from the accountancy profession in the 1930s and 1940s. Consistent with the theory of path dependence, the tendency for holding company directors to publish legal entity-based accounts (with or without adopting the equity method) can be considered shared by a number of holding company directors, institutionalised, and thus it became slow to change. Three areas that are important but not developed sufficiently in this study will be presented. Some limitations of this study will then be identified.

Chapter 2 Literature Review

2.1 Introduction

The main purpose of this chapter is to survey the existing literature concerning group accounting history in the UK. By doing this, this chapter aims at presenting the understandings of the topic achieved by the preceding literature and of the research question to be resolved in this thesis.

Section 2.2 deals with the prior empirical research which specifically focused on group accounting. First it will be observed that historical study on group accounting is important not only because of the two reasons stated in chapter 1 (it exemplifies an important case of accounting change and it represents a good example of difference of accounting between different countries), but also because contemporary studies on group accounting recognise the existence of very difficult problems concerning the functions and purposes of group accounting and it is meaningful to study group accounting in a different way, i.e. in a historical way. Second it will be revealed that the change in the UK from a single set of legal entity-based accounts to simultaneous publication of group accounts in addition to legal entity-based accounts has been well documented, but that the reason why it took so much time for change to occur has not been fully explained. This survey provides this study with the idea that the search for a more fundamental explanation can help obtain a better understanding on the development of group accounting in the UK.

Section 2.3 surveys the theoretically-inspired literature in order to identify the appropriate school of thought for this study to follow. This quest is important, because it is not easy, without a conceptual theory, to locate a particular cause as a fundamental element in bringing about a resulting effect. In other words, a theory-based explanation is needed for the purpose of providing a fundamental reason for why consolidated accounts were adopted only slowly in the UK. By undertaking the exercise of surveying the theoretically-inspired

literature, it will be shown that the most appropriate school of thought for the purpose of this study is described here as the 'recent Neoclassicism'. The dependence of this study on the recent Neoclassicism will be more fully explained in the next chapter along with the methodology of this study.

2.2 The empirical research

This section will deal with two types of previous literature concerning group accounting. First, contemporary studies on group accounting will be surveyed, because the problems raised by contemporary studies point to the need for historical research to provide a context for understanding and perhaps even resolving the issues, while historical studies need to be reviewed in order to contextualise the current work. Second, historical studies on group accounting in the UK will be surveyed in order to explain the importance of seeking for a fundamental answer to the unresolved research question: 'Why was the adoption of consolidated accounts slow in the UK?'

2.2.1 Contemporary studies on group accounting

Today, the term 'group accounts' is often used inter-changeably with 'consolidated accounts', but, in this study, the term encompasses six different methods which are classified in Edwards and Webb (1984) (for definitions of the six methods, see 4.4 in chapter 4). Among the six methods, this study mainly focuses on consolidated accounts and the equity method. The equity method is today used to account for associated companies and joint-ventures. However, 'in the U.K., the earliest use of the equity method appears to be for the purpose of including subsidiaries in the financial statements of investors as an alternative to consolidation' (Nobes, 2002: 18). Nobes (2002: 21) explains that 'this use of the equity

method in investor financial statements could be seen as an example of attempts by accountants to express commercial substance over legal form'. Also in the U.S., 'the equity method was used in parent company statements for certain subsidiaries' (Nobes, 2002: 18). Nobes introduces arguments by Kester (1918), which 'distinguished between parents which had "substantially full ownership" of subsidiary companies and cases where "ownership is not complete but still controlling", where the equity method in parent statements was seen as a reasonable alternative to the preparation of consolidated statements' (Nobes, 2002: 18). According to Nobes (2002: 20) the equity method can still be used in parent statements under U.S. regulation. In Netherlands, the use of the equity method in this context is used and it 'generally enables the equity of the parent to be equal to that of the group' (Nobes, 2002: 20). Nobes (2002: 21) further states that it is allowed and common in Denmark, it is allowed in France and Italy, but such permission is not granted in law in the U.K. or in Germany, where equity accounting is restricted to consolidated statements.

There are many previous works which have specifically dealt with consolidated accounts (Beckman, 1998a, b, 1995; Bierman, 1992; Casabona and Ashwal, 2005; Francis, 1986; Lowe, 1990; McKinnon, 1984; Neuhausen, 1982; Niskanen et al., 1998; Pendlebury, 1980; Rosenfield and Rubin, 1986) and the equity method (Burnett et al., 1979; Chasteen, 2002; Mazay et al., 1993; Nobes, 2002; Ricks and Hughes, 1985). Pendlebury (1980) and Francis (1986) reflect on whether consolidated accounts need to be supplemented by disaggregated information, saying that 'supplemental parent-only statements are necessary (at least in some situations) to avoid a significant loss of information due to the consolidation process' (Francis, 1986: 401-402). Francis concludes that 'the British and Australian approaches are superior to the American in that the information loss arising from consolidated reporting is reduced' (Francis, 1986: 394). Beckman (1988a) and Niskanen et al. (1998) compare information provided by parent-only earnings and by consolidated results.

Beckman (1998a) is a comparison of consolidated and parent-only earnings forecasts for Japanese firms, and Niskanen et al. (1998) examine the case of Finnish firms. Niskanen et al. (1998: 32) point out that 'parent company earnings ... are potentially informative to shareholders because of their linkage to dividends' since 'the dividends received by shareholders are based on current net earnings (and retained earnings from previous periods) of the parent company'. However, their results show that consolidated earnings 'convey information to owners, while parent-only earnings do not' (Niskanen et al., 1998: 38). McKinnon (1984) and Lowe (1990) deal with the question of whether consolidated accounts are suitable in different economic situations. McKinnon (1984) argues that the assumptions underlying consolidation practices in Anglo-American nations might be less appropriate to the corporate context in Japan. Similarly, Lowe (1990) asserts that Japanese consolidated statements do not represent the substance of the actual business relationships. Today's most tackled issue in the field is consolidation of special purpose entities (for example, FASB Interpretation No. 46 (FIN-46) issued in January 2003 and revised in December 2003[11]).

As for the equity method, Chasteen (2002) addresses the variety of equity methods available. In a similar vein, Nobes (2002) provides four descriptions of the use of the equity method. Burnett et al. (1979) show that the equity method was used as an alternative to full consolidation in America's 25 largest captive finance companies in 1970s, the selection of method being 'a function of management's preference' (Burnett, wt al., 1979: 823). Ricks and Hughes (1985: 51) demonstrate a 'support for the hypothesis that the market reacted to the new information contained in the added disclosures resulting from the change' from the cost method of accounting for long-term investments to the equity method, since 'income under the equity method ... includes the investor's share of the undistributed earnings of investee companies' (Ricks and Hughes, 1985: 36).

[11] This interpretation is criticised as 'many believe the standard-setting body has issued accounting guidance that is overly complex and is likely to result in financial statement distortions that were neither intended nor conceived of during the development of the interpretation. (Prescott et al., 2004: 18).

In general, these works seem to deal with the purposes/functions of consolidated accounts and the equity method (Beckman, 1995; Lowe, 1990; McKinnon, 1984; Niskanen et al., 1998; Nobes, 2002). It is true that the purpose of consolidated accounts is seemingly clear. For example, the following type of statement is widely made: 'consolidated accounts are prepared in order to show all group companies as if they are a single entity'. However, it is also known that present consolidation practice can not be explained from a consistent theoretical viewpoint[12]. And this involves technical issues such as the calculation of goodwill, minority interest and distributable profit. For example, under present practice, goodwill is recognised on the date the conditions for a parent-subsidiary relationship are met only in an amount equal to the difference between the parent's investment and its proportionate interest in the fair values of the subsidiary's identifiable assets and liabilities. The exclusion of goodwill for the part of minority shareholders is consistent with 'proportionate consolidation'. On the other hand, in the present practice, all of a subsidiary company's assets and liabilities are aggregated with the parent's assets and liabilities. This inclusion of assets and liabilities attributable to minority shareholders is consistent with the 'economic unit approach' (or 'entity theory'). The present consolidation practice is somewhere between the two extreme theories (economic unit approach and proportionate consolidation) and can not be explained from the perspectives of either of them[13]. It is said that if the purpose of consolidated accounts is aggregation of financial data of parent and subsidiary companies, consolidation procedure should follow the economic unit concept, and that if the purpose of consolidated accounts is the modification of the financial data of the parent company, consolidation procedure should follow, in a purely theoretical sense,

[12] The main works which deal with consolidation theory are Baxter and Spinney (1975 a,b), FASB (1991), Moonitz (1951). For example, Baxter and Spinney (1975a: 32) give 'a continuum of consolidation theories', 'the proprietary concept' at one extreme and 'the entity concept' at the other end. FASB (1991) uses a label 'proportionate consolidation' for the proprietary concept and 'economic unit concept' instead of the entity concept. Moonitz (1951) propose actual adoption of consolidation procedures based on the entity theory.

[13] See Baxter and Spinney (1975a: 32) and FASB (1991: paras. 63-65 and 114-118).

proportionate consolidation (FASB, 1991: paras. 63 and 64, Appendix 2, pp.34-35). However, it seems that there is no agreement as to what should be the purpose of consolidated accounts.

Unsettled debate can also be observed for the equity method. For example, Nobes (2002: 35) notes that 'although the equity method is now used for various purposes in much of the world, the rationales for this are not well explained'. He also writes that 'since the concept behind the equity method and the purpose of its use are unclear, it also becomes difficult to resolve technical issues' (Nobes, 2002: 37). For an example of unresolved technical issues, Nobes (2002: 37) raises the following question: 'when an investor makes a profit by selling to an associate which retains the goods (downstream sales), should some or all of the profit be eliminated from the investor's and the consolidated statements?' Inclusion or exclusion of minority interests becomes a matter here as well as in the consolidated accounts as stated above.

The research summarized above reveals the existence, in numerous settings, of very difficult problems to resolve concerning the functions and purposes of group accounting. It seems, therefore, potentially meaningful to study group accounting in a different way. That is, recognition of the existence of difficult problems requiring resolution justifies the historical approach for studying of group accounting, because 'the study of accounting history helps us to understand our past and gives us an appreciation of how our current practices and problems came into being' (Edwards, 1989a: 4) and moreover, 'the examination of past events ... enables us to appreciate the complexity and persistence of many of the problems presently facing accountants' (Edwards, 1989a: 6-7). The next sub-section of the study will survey preceding historical studies on group accounting.

2.2.2 Historical studies on group accounting in the UK

2.2.2.1 The analysis of accounting change

It has been already shown that the existing literature reveals the main historical events in the development of group accounting in the UK (see Table 1-1 of chapter 1). Five main events (Garnsey's lecture, the Royal Mail case of 1931, publication of Dunlop Rubber's accounts of 1933, the effect of RoAP7 and CA48) are thought to have caused consolidated accounts to become the principal form of group accounts.

First, Garnsey's lecture and his authorship of 'the first British book on the subject' (Edwards and Webb, 1984: 36) have been considered an important milestone in the history of group accounting. For example, Kitchen (1972: 114) noted that 'it is beyond doubt that the Garnsey lecture of 1922 was central to the development of accounting for holding company groups throughout the period with which we are concerned'. Further, again in Kitchen's words, 'The ICAEW Recommendation of 1944 ... which was effectively the basis of the Cohen Committee's recommendations of 1945 ... were essentially in line with Garnsey's lecture of more than a score of years earlier' (Kitchen, 1972: 118). Edwards and Webb noted that 'the main significance of Garnsey's lecture is that he set out the conventional wisdom of group accounting in a clear and concise manner, and he did so while a partner in a leading firm of chartered accountants during the course of a lecture delivered to the London members of the ICAEW' (Edwards and Webb, 1984: 37).

The second and third events that stimulated consolidated accounts to be widely accepted, namely the Royal Mail case of 1931 (*Rex v. The Royal Mail Steam Packet Company Case*) and publication of Dunlop Rubber's accounts of 1933,[14] have been the subject of significant prior discussion. Kitchen (1972: 134) considers the Dunlop Rubber accounts as

[14] Dunlop Rubber's accounts of 1933 are reprinted in *The Accountant* ('Dunlop's New Standard', 12 May 1934: pp. 676-9). The journal welcomes the accounts, saying 'it is almost impossible to find sufficient praise with which to acclaim the new standard in company accounting set by the 1933 accounts of the Dunlop Rubber Company Limited'.

'a real step forward in the standard of published group accounts'. Walker (1978a: 94) argues that 'it seems that the Royal Mail case was a major factor in encouraging the publication of consolidated statements'. Edwards (1989a: 232) refers to the Royal Mail case as it 'underlined some of the limitations of legal entity-based accounts and motivated some companies to publish consolidated statements' and also mentions Dunlop Rubber's accounts as 'a further impetus'. Specifically, concerning the Royal Mail case, the fact that dividends from subsidiary companies made the parent company's legal entity-based accounts appear misleadingly profitable is considered to have encouraged the publication of consolidated accounts (Walker, 1978a: 94).

Finally, the effect of regulations (such as the ICAEW's RoAP7 and the CA48) on British holding companies' group accounting practices and the initiatives taken by the accountancy profession have been investigated and considered important. The empirical studies conducted by Bircher (1988) and Arnold and Matthews (2002) reveal that the Royal Mail case and Dunlop Rubber's accounts were not the main factors in the development of group accounting in the UK. Their conclusion identifies the regulations as the most effective factor for the accounting change. For example, Bircher (1988: 12) finds that 'consolidated accounting only achieved widespread adoption in Britain after the Second World War in the shadow of legislation to enforce more comprehensive dissemination of group accounting information by holding companies'. Bircher (1988: 5) observes that only 22.5% of the sample holding companies had voluntarily adopted some form of consolidation accounts in 1938/39, which is after the Royal Mail case and publication of Dunlop Rubber's accounts. Similarly, Arnold and Matthews (2002: 9) find the proportion of companies presenting consolidated accounts to be 14.0% in 1935.

Concerning the comparative influence on the content of group accounts exerted by RoAP7 and by CA48, the previous literature has revealed that CA48 was more influential

upon British holding company directors' group accounting practices than RoAP7. According to Bircher (1988), there were only 32.5% holding companies in his sample which adopted consolidated accounts in 1944/45 (when RoAP7 was issued), whereas 74.0% companies published consolidated accounts in 1947/48 (when CA48 came into force).

2.2.2.2 The slow development

Accounting historians who have revealed the developmental process towards the publication of group accounts have wondered why, in spite of the factors which are described as driving forces in encouraging accounting change (Garnsey's lecture, the Royal Mail case and Dunlop Rubber's consolidated accounts), the change did not happen more promptly, especially when comparing the British situation with the case of the US. This irritation seems to have led them to make negative comments on the process.

Kitchen (1972: 114) described the process as 'the slow development in Britain' and further comments:

> But the Greene Committee's Report and the legislation of 1928-29 to which it led did not encourage innovation. The 1930s had begun before the accounts sections of the 1929 Companies Act were fully effective. In mid-1931 there was the Kylsant case, which started everybody thinking afresh. Still, changes after Kylsant were not immediate, and the positions taken up in the years 1922-26 were not generally vacated until 1934 or later. (Kitchen, 1972: 134)

Parker (1977: 206) also stated that 'Progress [in Britain] was much slower than in the United States', and that 'Both the need for the new technique and its recognition came more slowly in Britain than in the United States'. Edwards (1989a: 230) similarly stated that 'The rate of adoption of group accounting procedures was slow, particularly compared with the US where, by 1910, consolidated accounts were a common feature of financial reporting'.

The negative comments on the rate of development of group accounting in the UK are not confined to today's accounting historians, but are also found in views expressed by

accountants at the time. For example, Dickinson (1924: 272) commented on the positions in Britain and the US as follows:

> In one particular the accounts published by American companies are much in advance of those published in Great Britain, and that is in the case of holding companies so called, *i.e.* those which hold all the shares in a large number of operating companies. In the United States the almost universal practice for more than fifteen years past has been to publish for such companies a consolidated statement of the earnings, and a consolidated balance-sheet aggregating the assets and liabilities of all the subsidiary companies and eliminating the investments therein of the holding company ... The practice in Great Britain is in its infancy, and only a few concerns have yet adopted it ... (Dickinson, 1924: 272)

The next part surveys the reasons given in the previous literature to try to explain why British accountancy made 'slow progress' concerning group accounting.

2.2.2.3 The reasons for slow change

Several writers have identified forces generating resistance to change in respect of consolidated accounts. Edwards and Webb (1984) provided the most comprehensive comments on the reasons for 'slow progress'. They suggested the following six factors as affecting the development of group accounting in the UK up to 1933, though they cautioned readers that 'a full explanation ... is not attempted in this paper' (Edwards and Webb, 1984: 41-7).

> *Technical Competence* ... it was not until 1925 that questions which required candidates to prepare a consolidated balance sheet were regularly included. The absence of readily available texts which could be used by students preparing for their examinations ... and the lack of available material is the subject of correspondence in *The Accountant* in 1935.
> *Demand for Group Accounts* ...The information requirements of the British public do appear to have been less demanding than those of its American counterpart.
> *Management Opposition to Disclosure* ... The general reluctance of British management voluntarily to publish group accounting information is an important factor explaining the relatively slow rate of adoption of those procedures in Britain as compared with the United States ... Subsidiary companies [not consolidated] provided considerable scope for smoothing the holding company's trend of reported profits.
> *The Accountants' Reluctance to Innovate* ... The British profession, possessing a longer tradition and, in its view, a more professional and less commercial attitude towards accounting, may well have been unreceptive to ideas developed [in the United States] ...
> *Legal Barriers* ... it does seem that CA 1908, Section 26(3), implied a legal obligation for

> directors to deliver a legal entity based balance sheet to the Registrar.
> *Creditors' Requirements* ... Creditors usually enter into contracts with the *company* and their claims will be restricted to the assets of the legal entity which has received the money or goods. (Edwards and Webb, 1984: 41-7)

The first reason given by Edwards and Webb, technical competence, is similarly commented on by Parker. He (1977: 207) stated that 'Consolidation accounting is neither simple nor easy to try on a limited basis' and 'Nor is it easily observed and described, though certainly the technical ability was readily available in the larger accounting firms'. In addition, Kitchen (1977: 135) noted that the First World War resulted in little time for qualified accountants who remained in the profession to try out new techniques.

The second reason, less demand for group accounts, was also mentioned by Kitchen. He (1972: 114) stated that 'at the beginning of the 1920s, the holding company group was still a relatively new phenomenon in this country, though it was already well established in North America'. Hein (1978: 272) also mentioned that 'holding companies or parent-subsidiary groupings did not play a significant role in business organizations in Britain'. Garnsey (1923: 59) provided another viewpoint, observing that 'in view of the fact that the shares in the industrial concerns of this country are generally very widely distributed among a large number of shareholders, the call for the consolidated accounts has never been insistent'. Parker (1977: 206-7) attributed less demand for group accounts to British cultural values, stating that 'A change in accounting practice was less compatible with the cultural values of the British social system'.

Management opposition to disclosure is often focused upon by accounting historians when discussing 'slow progress' in the UK compared with the US (Bircher, 1988: 11; Edwards and Webb, 1984: 43; Garnsey, 1923: 59; Parker, 1977: 207). It seems that the most influential writing on this subject was provided as early as 1923 by Garnsey.

> Perhaps, ... the greatest opposition to any but the most essential changes in the form of the published accounts comes from directors who are not all imbued with the desire of giving

their shareholders as much information as possible, no doubt having in mind the necessity for avoiding disclosure of information which might conceivably be of use to competitors. (Garnsey, 1923: 59)

Edwards and Webb's (1984: 44) focus on the directors' desire to smooth the holding company's trend of reported profits is shared by Bircher (1988: 11). Garnsey (1923: 18) also stated that 'it [a legal entity-based balance sheet] admits of the equalisation of the income of the parent company from one period to another by the retention of undistributed profits in the accounts of the subsidiaries'. Kitchen provides a broader explanation for management opposition to disclosure, stating that 'Many business men, particularly industrialists and directors of large undertakings, felt themselves hard-pressed and on the defensive, surrounded by more or less hostile faces, whether of creditors, competitors, shareholders, labour, government, or the public' and that 'To many of them, to increase disclosure seemed tantamount to inviting more criticism – at the least more questions, and many had had their fill of inquiries' (Kitchen, 1972: 135).

As the fourth possible explanation for the observed slow rate of accounting change, Edwards and Webb (1984) noted that professional rivalry between the UK and the US accountants might have resulted in the former's reluctance to adopt a reporting framework developed by the latter. In a similar vein, Garnsey (1923: 59) noted that 'the natural reluctance of the people of this country to change is too well known to require any comment'.

The fifth reason, legal barriers, was first put forward by Dickinson in 1924. He (1924: 273) considered that 'one obstacle to the general adoption of the principle of the consolidated balance-sheet is that in the present state of the law it is not the legal balance-sheet of the company, and it is consequently necessary to prepare and file the ordinary balance-sheet as well as the more accurate consolidated one'. According to him (1924: 273), 'In the United States this difficulty does not arise, as there are no statutory provisions as to the form of balance-sheet for ordinary commercial companies, nor are they

required to be published, while the federal tax Laws call specially for a consolidated statement of earnings'.

The sixth reason, creditors' requirements, can be traced back to D'Arcy Cooper (1925a), who stated that 'So far as the interests of creditors are concerned, it is a fallacy to suppose that they would be better informed [by an amalgamated or consolidated balance sheet]: they would only be misled, because the creditors of one company have no claim upon the assets of another company'.

Based on Edwards and Webb (1984), the above is not an exhaustive list of explanations for slow development in the UK. Kitchen (1977) drew attention to Garnsey's relative youth (he was forty when the first edition of his book was published) and his association with civil servants and governmental and quasi-governmental institutions and enquiries. Kitchen (1977:115) suggested that these facts 'made him something less than perfectly acceptable in the early 'twenties as a man able to speak for the accountancy profession, at least in the eyes of its more traditionally minded members'. Kitchen (1977: 135) made the further point that 'the accountancy profession [at the time] was aware that the form of a company's accounts is a matter for the directors'.

2.2.2.4 The need for a more fundamental explanation

It is true that the above observations all have potential to explain the resistance to change in the development of group accounting in the UK, though the writers often acknowledge doubts concerning their likely importance in practice. For example, concerning the issue of technical competence, Edwards and Webb (1984: 42) note that 'the aggregation of the results of departments and self accounting branches, in order to produce legal entity-based reports was a routine accounting process'. More generally, as noted in chapter 1, the following fundamental question was raised by researchers such as Kitchen (1972) and Bircher (1991)

even after the writers had carefully and deeply examined the matter: Why was the adoption of consolidated accounts slow in the UK? The provision of an answer to this question is the purpose of the present study.

For this purpose, this study intentionally steps back from the six or more reasons presented in the previous literature. This does not mean that such reasons are irrelevant in explaining the slow change, but it seems clear that they are not enough. It seems an opportune time, following the many contributions of previous researchers, to attempt a theoretically informed explanation for the slow adoption of consolidated accounts in the UK. The support provided by a theoretical framework is important, because it is otherwise difficult to clearly relate one thing to another from the available sources of evidence, especially in terms of a relationship of cause and effect.

However, it is not self-evident which conceptual theory is appropriate for the purpose of this study. The second half of this chapter will be devoted to identifying which school of thought the present study should rely on.

2.3 The theoretically-inspired literature

The growth of interest in historical methodology (Edwards, 2004; Walker, 2006: 109) is important for a research thesis which aims to provide a theoretical perspective for an archival-based study of the development of group accounting in Britain in the first half of the twentieth century. This section (2.3) surveys the theoretically-inspired accounting history literature before moving on to consider its significance for the theoretical approach employed in this thesis (chapter 3).

2.3.1 Discussion over methodological issues

Edwards (2000: Introduction, xxxiv) notes that 'A significant feature of the study of accounting history in recent years has been the emergence of a widening range of theoretical approaches'. The collection of research studies which he edited (Edwards ed., 2000) starts with 'nine papers that explore the range of different ways of conducting historical research' (Introduction, xxv). These papers are all concerned not with a specific point of time and space in accounting history but with wider and broader methodological issues such as how to conduct historical research or what is historical study. Indeed, the first article provides 'a roadmap that makes this [historical] research activity accessible' (Fleischman, Mills & Tyson, 1996: 4). The second and third articles, a pair of papers written by the same authors (Previts et al, 1990a, 1990b) and published in consecutive issues of *Abacus*, also focus on broad issues such as the definition, relevance, subject matter and methodology of accounting history. The fourth article (Parker, 1993) raises an issue that has subsequently received much attention (Carmona and Zan, 2002; Carmona, 2004, 2006), namely that 'the writing of accounting history is increasingly dominated by writers in English discussing private-sector accounting in English-speaking countries of the nineteenth and twentieth centuries' (Parker, 1993: 68). The next three articles are also involved with methodological debates, and are summed up by the editor as follows:

> Johnson (1975) makes the case for the use of a Chandlereseque analysis by accounting history researchers to help comprehend the development of the modern business enterprise. Johnson is a traditional historian; that is, he is part of the group that 'new' accounting historians judge to be preoccupied with tracing accounting's history as one of continuous evolution, technical elaboration and improvement towards its present state. This method of studying accounting's past was critiqued, in 1987, by a leading architect of 'The new accounting history', Anthony Hopwood. ... Hopwood therefore encouraged an examination of accounting over time through a consideration of the preconditions for change, the process of change and its organisational consequences. (Edwards, ed., 2000: introduction, xxv-xxvi)
>
> Even more trenchant criticism of much prior work by accounting historians is contained in Miller and Napier (1993). ... The paper argues for a recognition of the historical

> contingency of current practices, an awareness of the significance of the discursive nature of the calculation, the language and vocabularies in which a particular practice is articulated, and a focus on 'ensembles' of practices and rationales rather than isolated instances of this or that way of doing accounting. (Edwards, ed., 2000: introduction, xxvi)

The last two articles also deal with methodological issues, both calling for understanding between accounting historians in conflict. For example, the eighth paper (Funnell, 1996) shows that there are common grounds between 'new' and 'old' accounting history by exploring such terms as 'facts', 'interpretation', 'reality' and 'narrative' and the ninth paper (Carnegie and Napier, 1996: 176) is based on a recognition that 'Mutual reliance (often unacknowledged) between the traditional and new historians of accounting may be seen in the propensity of new historians to rely heavily on the archival discoveries of the traditionalists, who themselves often find their work enriched by an awareness of the conceptual debates of the new historians'.

Similarly, the compendium of prior-published research papers edited by Fleischman (2006) starts with articles concerning methodological matters. The first part of the compendium consists of eight articles, being arranged to give 'an overview of the participants and themes of the historical discourse which is to follow' (editor's introduction, xxxi). The first of these was intended to distinguish three types of methodology in accounting history as outlined by the author as follows:

> Three main strands of historical accounting research have been examined. First, the traditional type of research, motivated, at best, by a desire to understand the past, was examined. ... The paper then examined two recent developments in historical methodology which are quite different in their approach. These are the socio-historical approach to studying accounting in the contexts in which it operates, and positive historical research. (Napier, 1989: 14)

Similarly, it is clear that the second and third articles deal with methodology since they refer to 'a pluralistic approach that includes serious intellectual research and debate amongst and within various theories, ideologies and methodologies' such as 'Neoclassicism',

'Foucauldianism' and 'Marxism' (Fleischman, Kalbers and Parker, 1996: 37) and 'Habermas's Methodological Positions' (Lodh and Gaffikin, 1997: 55). The fourth article advocates new accounting history which embraces 'the pluralization of methodologies' (Millar, Hopper and Laughlin, 1991: 87). The other articles discussed: 'theoretical and methodological perspectives for critical accounting' (Laughlin, 1999: 98); 'the issue of methodological transference to assess how comparative world views impact interpretation of research results in behavioural accounting research' (Merino and Mayper, 1993: 105); the 'exploring and augmenting [of] the assumptions, concepts and methodologies employed by historians in their understanding and utilisation of time in accounting and management history research' (Parker, 2004: 127); and 'the various accounting historiographical paradigms' (Oldroyd, 1999: 153).

Thus it is obvious that there are many important discussions of accounting's historical methodology in recent years. Moreover, the growing diversity of methodologies applied to studies of accounting history has been accompanied by the application of a variety of theoretical approaches which encompass a range of social science disciplines[15]. For the purpose of this study, the three schools of thought which have been widely applied in accounting history will be surveyed in the next sub-section (2.3.2). By doing this exercise, it will become clear which school of thought might be most appropriate for this study to follow in explaining the slow adoption of consolidated accounts in the UK in the first half of twentieth century.

[15] Lodh and Garrikin (1997: 46) summarised several alternative theoretical approaches such as (a) symbolic interactionism and ethnomethodology, (b) political economic (including Marxian) approaches, (c) Habermasian critical theory, (d) Foucauldian approach, (e) Giddens's structuration theory, (f) Gramsci's concept of hegemony, (g) Derrida's deconstructionism, (h) social constructionists, (i) critical structuralists, (j) technoscientists' approaches such as actor-network theory in studying 'accounting–in–action'.

2.3.2 Three schools of thought in accounting history

2.3.2.1 Neoclassicism/Foucauldianism/Marxism (labour process)

There are three principal schools of accounting thought which are, today, applied to accounting history; the Neoclassical, Foucauldian, and Marxist/labour-process paradigms. Fleischman and Radcliffe comment that the Neoclassical or economic rationalist perspective as 'traditional' and Foucauldian and Marxist/ labour process as 'critical' theorists as follows:

> Recently published writing on the history of accounting generally has focused attention on three major research paradigms or 'worldviews'. For many years the Neoclassical or economic-rationalist perspective has dominated as the main stream, traditional approach. More recently, this privileged position has come under challenge from critical theorists whose voices are now being forcefully heard. The schools represented here are the Marxist/labour process, from a tradition older even than Neoclassicism, and the Foucauldian, a product in the first instance of French postmodernism. It has been recognized previously[16] that critical historiography is vastly wider than these two, but Marxism and Foucauldianism have been the most prominent. (Fleischman and Radcliffe, 2003: 12)

The prominence of these three research paradigms is also assessed by other researchers (Boyns et al., 1997; Fleischman and Parker, 1997; Loft, 1991). Table 2-1 compares the names that these four publications attach to the three schools of accounting thought. For example, the Neoclassical paradigm is variously described as 'The Johnson and Kaplan school' (Loft, 1991: 18, 37), or 'Economic determinist' (Boyns et al., 1997: 178), or 'Neoclassicism' (Fleischman and Parker, 1997: 250; Fleischman and Radcliffe, 2003: 13). This study employs the wordings offered by Fleischman and Radcliffe (2003): 'Neoclassicism', 'Foucauldianism' and 'Marxist/labour process'.

[16] Fleischman and Radcliffe (2003: 9-11) mention several alternative theoretical approaches of critical historiography, which include Marxism (labour process), Foucauldianism, Habermasianism, Derridian deconstructionism, Gramschism. Miller et al. (1991: 397) introduce Thomas Kuhn, Clifford Geertz, Michel Foucault, E.H. Gombrich, Eric Hobsbawm, Paul Ricoueur, Richard Rorty, Charles Taylor, E.P. Thompson and Peter Winch as influential writers in broadening the discipline of history.

Table 2-1 Three schools of thought

Literature	*Three principal schools of thought in accounting history*
Loft, 1991*	• The Johnson and Kaplan school relying on economic theories • Critical studies using insights from Foucault • Labour-process school/critical studies using insights from Marx
Boyns et al., 1997	• Economic determinist • Foucauldian • Marxist
Fleischman and Parker, 1997	• Neoclassicism/economic rationalism • Foucauldianism • Marxism/labour process
Fleischman and Radcliffe, 2003	• Neoclassicism/economic rationalism • Foucauldianism • Marxism/labour process

*Loft (1991) specifically deals with management accounting history research.

Sources: Loft (1991), Boyns et al. (1997), Fleischman and Parker (1997), Fleischman and Radcliffe (2003)

Foucauldianism and Marxism are often presented as 'new' or 'critical' accounting historical paradigms, whereas Neoclassicism is considered as the 'old' or 'traditional' paradigm. In a paper which introduced the highly acknowledged special issue on 'The new accounting history' in *Accounting, Organizations and Society*, Miller, Hopper and Laughlin, describe the common character of 'new' accounting historical paradigms as:

> a proliferation of methodologies, a questioning of received notions such as progress and evolution, a widening of scope, a new attentiveness to the language and rationales that give significance to accounting practices, and a shift of focus away from invariant characters such as the book-keeper and the decision-maker towards a concern with broader transformations in accounting knowledge (Miller et al., 1991: 395).

Although Fleischman and Radcliffe (2003: 2) distinguish old/new and traditional/critical dichotomies, the terms 'new' and 'critical' accounting history are often used interchangeably (Boyns and Edwards, 2000: 151; Fleischman and Radcliffe, 2003: 4). In Fleischman and Radcliffe's words (2003: 4), 'while each brings different nuances, there is general agreement as to the body of work that is referenced'. This study also treats the terms 'new' and 'critical' accounting history as interchangeable. Consistent with this, the terms 'old' and

'traditional' accounting history will be used in the same way. Therefore it is understood in this study that Foucauldianism and Marxism represent 'new' and 'critical' accounting and that Neoclassicism represents 'old' and 'traditional' accounting.

In order to locate more specifically the characteristics of the three schools of accounting thought, prime advocates of each school are derived from an examination of the four works presented in Table 2-1. The results are given in Table 2-2.

Table 2-2 Prime advocates in three schools of thought

	Prime advocates in three schools of thought		
Work	*Neoclassicism*	*Foucauldianism*	*Marxism/labour-process*
Loft, 1991	Johnson & Kaplan, 1987	Miller & O'Leary, 1987 Loft, 1986, 1990 Hoskin & Macve, 1986, 1988	Tinker, 1985 Armstrong, 1985, 1987 Neimark & Tinker, 1986 Hopper, et al. 1987 Hopper, 1988
Boyns et al., 1997	-	Miller & O'Leary, 1987 Miller & Napier, 1993 Hoskin & Macve, 1986, 1988, 1994 etc Loft, 1986, 1990	-
Fleischman and Parker, 1997	Johnson & Kaplan, 1987 Johnson, 1981, 1986	Hoskin and Macve, 1986, 1988 Hopwood, 1987 Walsh and Stewart, 1993	Tinker, ed. 1984, Tinker, 1985, 1991 Tinker & Neimark, 1988 Neimark, 1990 Tinker et al. 1991
Fleischman and Radcliffe, 2003	Johnson & Kaplan, 1987 Rochester school of accounting positivists Edwards, 1989b Edwards & Boyns, 1992 Edwards et al., 1990 Fleischman & Parker, 1990, 1991	Burchell et al., 1980, 1985 Hopwood, 1988 Hoskin & Macve, 1986, 1988 Miller & O'Leary, 1987 Walsh & Stewart, 1993	Bryer, 1994a, 1999 Hopper & Armstrong, 1991

Sources: Loft (1991), Boyns et al. (1997), Fleischman and Parker (1997), Fleischman and Radcliffe (2003)

The advocates that are most commonly recognised among the four works are Johnson and Kaplan (1987) for the school of Neoclassicism, Miller and O'Leary (1987) and Hoskin and Macve (1986, 1988) for Foucauldianism, and the works by Tinker, Armstrong and Hopper for

Marxism. One other feature of this selection is that most of the works cited are on management accounting research. Johnson and Kaplan's work is entitled *Relevance Lost: The Rise and Fall of Management Accounting.* Miller and O'Leary (1987) are concerned with the emergence of standard costing and budgeting in the early decades of the twentieth century. Hoskin and Macve (1988) suggest that the pre-eminence of the U.S.A. in the development of cost and management accounting can be traced to the influence of the engineering graduates of the military academy at West Point. Hopper and Armstrong (1991) give a criticism of Johnson and Kaplan's work under the title of 'Cost Accounting, Controlling Labour and the Rise of Conglomerates', by 'considering accounting developments in the light of labour process histories of capitalist organisation'. It therefore seems clear that the three schools of accounting historical thought have been mainly concerned with management accounting research rather than with financial accounting.

2.3.2.2 Exploring use of the three schools of thought to study financial accounting history

It was noted that much new/critical accounting history focuses on management accounting research, but at the same time there are studies in the field of financial accounting among the advocates listed on Table 2-2. Below, the three approaches towards research in financial accounting will be outlined in order to assess which appears most appropriate for the present study of the development of group accounting in the UK in the first half of twentieth century.

Within the field of financial accounting, Fleischman and Radcliffe (2003: 14) classify (Table 2-2) the Rochester school of accounting positivists as advocates of Neoclassicism[17]. These include famous works such as Watts (1977), Zimmerman (1979) and Watts and Zimmerman (1978, 1979). Although some have criticised the methodology (e.g.

[17] According to Fleischman and Parker (1997: 251) and Fleischman and Radcliffe (2003: 13), the most influential economic literature to the Neoclassicism in accounting history were Coase (1937), Williamson (1971, 1973, 1975, 1985), Alchian & Demsetz (1972), Fama (1980) and Jensen & Meckling (1976) and Chandler (1977).

Christenson, 1983), these works are considered by many to have provided an effective foundation for a theory of financial statements adopting an agency relationship. The concept of an agency relationship was pioneered by Jensen and Meckling (1976), where an agency relationship is defined as 'a contract under which one or more persons (principal(s)) engage another person (the agent) to perform some service on their behalf which involves delegating some decision making authority to the agent' (Jensen and Meckling, 1976: 308). Applying the concept to the study of financial accounting, Watts (1977: 55) explains that 'the relationship between shareholders and managers is an agency relationship' with shareholders as principals and managers as agents.

Under the agency relationship, Watts and Zimmerman assume that 'the function of audited financial statements in an unregulated economy is to reduce agency costs' (Watts, 1977: 58; Watts and Zimmerman, 1979: 277)[18]. Agency costs are comprised of three different costs: the principal incurs expenditures to control the agent's behaviour (monitoring expenditures by the principal); the agent incurs expenditures to guarantee that he will not take certain actions to harm the principal's interest or that he will compensate the principal if he does (bonding expenditures by the agent); but even with monitoring and bonding expenditures, the actions taken by the agent will differ from the actions the principal would take himself (the residual loss) (Watts, 1977: 56). It is positive accounting's main assumption that company accounts are prepared in order to reduce the agency costs.

None of the Foucauldian-inspired research listed in Table 2-2 focuses on financial accounting. The reason can be perhaps understood from the underlying methodology of the school. The essence of Foucauldianism in accounting history is explained by Loft (1991: 30) as follows:

[18] As the citation shows, Watts (1977) and Watts and Zimmerman (1979) emphasise that their framework of agency theory is applied in an 'unregulated' economy. However, it seems possible to consider that the framework could be used for 'regulated' situations as well, because, as Coombs and Edwards (1996: 4) describe, regulations and market forces can be seen as 'two mechanisms as a means of explaining changes' which can co-exist, rather than as alternatives which exclude each other.

> In his book *Discipline and Punish: The Birth of the Prison* (1977) Foucault uses the history of prisons as an exemplar of a society-wide phenomenon occurring from the late eighteenth century onwards: the growth of 'disciplinary institutions'. Prisons, armies, hospitals, schools, mental institutions and factories all have in common that within them people are arranged and grouped into different categories – for instance, in the school according to their age and ability, in the hospital according to type of illness, and in the factory according to function. Even more importantly, they are arranged so that they can be watched and punished if they do not obey the rules, hence the phrase 'disciplinary institutions', in which 'disciplinary techniques' are practised. The term 'disciplinary techniques' covers a wide variety of methods of watching and controlling, including the recording of people's work, the progression of their illness, and also the architecture of buildings themselves, which gives a clear space in which everything can be seen. (Loft, 1991: 30)

The main attempt in applying Foucault's work to accounting history embraces an assumption that 'the history of closed institutions (asylums, prisons, barracks, schools) appears in many ways to parallel the factory system and other facets of modern life in which accountancy is implicated' (Fleischman and Radcliffe, 2003: 15). It is beyond this study to examine the assumption, but the concept of closed institution may be rejected as inapplicable to capital market research, which is a main focus in the studies of financial accounting[19].

Turning attention to the labour process paradigm, it is well known that Marx's arguments on capital markets have been long discussed among academics (for example, Hilferding, 1910), and Bryer (1994b, 1999), both these publications are listed in Table 2-2, specifically focuses on financial accounting. Bryer's works depend on a Marxist framework that classifies and characterises the long historical process into such stages as 'slavery', 'feudalism' and 'capitalism' (Bryer, 2005: 32). At the stage of capitalism, according to the Marxist view, the capitalist mentality had arisen that 'drove farmers, and then landlords, manufacturing entrepreneurs and ultimately managers, to constantly "improve" production; to continuously increase the intensity and productivity of labour to earn an excess return on capital' (Bryer, 2005: 30). In the late nineteenth century, as industrial companies became

[19] This does not mean, of course, that Foucauldianism has no potential for explaining the historical process of financial accounting.

collectively owned, the collective needs of investors who held the capitalist mentality gave rise to modern financial reporting (Bryer, 1993), because 'the general rate of profit provides capital with collective control of production' (Bryer, 1994b: 315). Bryer distinguished the Marxist's view as 'investor capitalism' from the dominant view of 'managerial capitalism'[20] (Bryer, 1993).

Marxism tries to explain historical development from three elements (social relations of production, calculative mentality and accounts) as follows:

> Social relations of production are a society's modal relations of economic superiority and subordination that condition the way owners of the means of production extract surplus value from labour. This makes accounting central to understanding and testing Marx's theory because rationalising each set of social relations - each way of extracting surplus – is a particular calculative mentality and a mode of accountability. The feudal mentality pursued the direct appropriation of surplus labour (labour itself, commodities or cash) from self-sufficient peasants, and feudal landlords and merchants kept income and expenditure accounts. The capitalist mentality pursues the rate-of-return on capital employed in production by extracting surplus value from the sale of commodities or services produced by wage labour, and the capitalist keeps balance sheets and profit and loss accounts. (Bryer, 2005: 28)

Above, three schools of thought were surveyed in order to find which school appears the most appropriate for this study to rely upon. Future research may reveal the potential for applying the ideas of Foucault and Marx to the study of the history of financial accounting. For the present, however, and for the reasons stated below, recent Neoclassicism is considered most likely to provide a fundamental and theoretically-derived answer to the research question posed in this thesis. The first reason is that a preceding work on the development of consolidated financial reporting in Australia (Whittred, 1986) adopted the Neoclassicism paradigm, though implicitly, by focusing on the relationship between company directors and the financial markets. The second reason is that the recent Neoclassicism is attractive because it accepts some important aspects of 'new' accounting history and seems to achieve a

[20] The Neoclassicism in financial accounting takes position of 'managerial capitalism' and on this point the Neoclassicism and the Marxism disagree each other. For example, Watts and Zimmerman (1978: 113) state that 'Management, we believe, plays a central role in the determination of [financial reporting] standards'.

case of 'confluence' (Fleischman and Radcliffe, 2003: 21) and 'conciliation' (Fleischman, ed., 2006: editor's introduction, xxviii) of the three schools of thought. For example, it accepts social and cultural factors as well as an economic factor as impetus for accounting change, and it does not necessarily see accounting development as 'progress'. The next sub-section will argue this point.

2.3.3 The recent Neoclassicism

As the most applicable approach for the study on the development of group accounting in the UK, the recent Neoclassicism is focused upon in this thesis. As Table 2-2 indicates, Fleischman and Radcliffe (2003) include Edwards (1989b), Edwards and Boyns (1992) and Edwards et al. (1990) in the category of Neoclassicism, along with Rochester school of accounting positivists. This categorisation seems reasonable as Boyns and Edwards (2000: 153) themselves state that 'we would locate ourselves within Loft's "neoclassical revisionist" school'. In this study, in order to distinguish them from Rochester school, the term 'recent Neoclassicism' will be used.

Unlike the other schools of thought surveyed above, the recent Neoclassicism does not claim to supply a 'grand theory' of accounting history, in the sense that it does not profess to provide an overall and exclusive explanation of historical developments. However, it does seem that the recent Neoclassicists share with other schools of thought some basic ideas concerning accounting history research. Below, it will be discussed that the basic ideas of the recent Neoclassicism are identical to that of Rochester school of accounting history in that both utilize a framework of supply/demand or need/response relationships[21], but that the basic

[21] Similar to Watts and Zimmerman, Edwards and Boyns employ the demand-supply or need-response framework. Under an agency relationship, shareholders demand company accounts and managers supply company accounts in order to reduce the agency costs. Similarly, Edwards and Boyns adopt the demand-supply framework in describing an accounting change in history. For example, Boyns and Edwards (1996: 57) note that 'entities can change accounting practices in response to pressing needs'. For another example, Carnegie and Edwards (2001: 303) explicitly state that 'efforts to achieve closure [of the accountancy profession] have

ideas of the recent Neoclassicism are different from the agency theory-based accounting history in three senses. First, the recent Neoclassicism takes broader context into consideration than the simple relationship between shareholders and managements. Second, the recent Neoclassicism makes the point explicitly that the notion of progress is inappropriate for the study of accounting history. Third, they emphasise the importance of not only an explanatory theory but also archival evidence. It will be declared that this study relies on the view held by the recent Neoclassicism, because the three points achieve the consensus of the three schools of thought which were surveyed in 2.3.2 and increase attractiveness of the Neoclassicism.

2.3.3.1 Understanding through broader contexts

The three points of difference between recent Neoclassicism and the Rochester school, identified at the end of the previous section, will be discussed in turn (sub-sections 2.3.3.1, 2.3.3.2, and 2.3.3.3). It will be also be revealed that the three distinctive features of new Neoclassicism are shared by most new/critical accounting historians concerning how accounting history research should be conducted.

The recent Neoclassicism agrees that studies of accounting's history should take into consideration broad contexts such as economic, political, social and cultural elements. The exclusive attention of historical studies on economic elements as explanatory factors – Watts and Zimmerman's (1978) agency based explanation would fall into this category – has been criticised by the 'new' and 'critical' accounting historians. As Laughlin puts it:

First and foremost critical accounting is always contextual. It maintains that accounting,

---

naturally exploited the potential provided by *both demand side* (for example, lobbying for State preferment) *and supply side factors*' (*emphasis added*).

> whether as a practice or as a profession, is a phenomena [sic] which has social, economic and political consequences and needs to be understood (and changed) in this context. (Laughlin, 1999: 97)

Miller, Hopper and Laughlin (1991: 87) also describe that traditional accounting historians have been 'viewing the history of accounting as a natural evolution of administrative technologies'.

However, not all the Neoclassicist literature ignores the social and political contexts. The recent Neoclassicism does not adopt a purely 'economic rationalist' stance. While adopting a mainly economic rationalist stance in their work on management accounting, Boyns and Edwards (2000: 153) 'nevertheless accept that economic factors might not be the only ones influencing the adoption of particular practices or modes of accounting at specific points in time or space'. They explicitly take into consideration not only economic factors but also socio-political contexts (Boyns et al., 1997: 6).

By accepting the idea that economic factors might not be the only ones influencing the adoption of particular accounting practices, it can be said that Edwards and Boyns create a bridge between the 'old' and 'new' accounting history, whilst improving the attractiveness of the Neoclassicist approach. In other words, they proposed a balanced view of accounting history[22], which is broader than the Neoclassicism that dealt only with economic interests and the Foucauldianism which tended to exclusively refer to 'power-knowledge' elements. Boyns and Edwards (1996: 57) state that 'while we can accept the need to examine supply-side influences, including power-knowledge, we do not see this as being incompatible

[22] It can be noted here that taking into consideration socio-political contexts as well as economic factors is not a new idea for accounting historians. For example, Brundage (1951: 79-80) suggests six milestones in accounting history which include social factors such as government regulation of accounting in 1907, high taxation during World War I, adoption by the New York Stock Exchange of standards of accounting disclosure in 1932, emphasis on accounting during World War II, and postwar developments in accounting due to inflation and enhancement of the position of organized labor and farmer. Peloubet (1953: 13) also recognises that accounting is a product of organic phenomenon: 'accounting, in and of itself, is little more than a series of not particularly complicated equations and mathematical rules and concepts; while the real importance of accounting, its difficulties, its complications and its possibilities for contribution to the social, economic and business life of the country lie in the application of these formulas and concepts to the description, analysis and interpretation of actual and present facts and conditions'.

with views which also acknowledge the possible influence of demand-side, or economic rationalist, influences'. The importance of recognising the possibility of multiple explanations as well as the need to be mindful of the limitation of documentary sources is made by Coombs and Edwards (1995: 104). Edwards' view on accounting development provides a further example which bridges between the 'old' and 'new' accounting history:

> Accounting did not develop into its present state in a straight-forward and orderly fashion. Major changes have usually been achieved as the result of numerous pragmatic adjustments to new circumstances. Each era produced different environmental conditions and imposed new demands on accounting. A proper understanding of accounting developments therefore requires a careful examination of the interrelationship between accountants and accounting techniques on the one hand and, on the other, the social and economic context in which the changes took place. (Edwards, 1989a: preface)

It is reasonable to conclude that the recent Neoclassicism thinks it necessary to understand the history of accounting within the broader contexts.

2.3.3.2 The notion of 'progress' is inappropriate

The second fundamental aspect of the recent Neoclassicism is that the notion of 'progress' is an inappropriate standpoint for the study of accounting's past.

Such caution is of course explicitly demanded by so-called new accounting historians. For example, 'the new accounting history can also entail a certain scepticism concerning the applicability of notions of "progress" and "evolution" to accounting history' (Miller, Hopper and Laughlin, 1991: 91). For another example, Napier (2001:7) noted as follows:

> It seems plausible to say that there is an agreed view among both new and traditional accounting historians that 'from a social science perspective, progress is a problematic concept, as it implies not just change but also improvement, and thus seems to imply the making of a value judgement' (Napier, 2001:7).

Part of the reason why the literature has tackled this issue is because of concerns that accounting historians did sometimes see accounting's past as a history of achievement – of

individuals and institutions striving to make accounting better, with the present state representing the pinnacle of achievement to date. For example, Hopwood (1987: 208) states that 'for until recently, most historical analyses of the accounting phenomenon, if not adopting a quite atheoretical stance, have been content to see accounting change as a process of technical elaboration and, almost invariably, improvement'. Focusing on the early professionalisation literature, Edwards (2001: 676) agrees that 'earlier [i.e. pre-new accounting history] work, in the main, described the relatively unproblematic rise of the accountancy profession as a means of meeting the needs of an increasingly industrialized society'. But this was not an invariable feature of even early studies of accounting's history. Nor is it certain that the idea of progress in accounting history, when it emerges, is confined to traditional historians. For example, it is not entirely clear whether Marxism employs or rejects the term such as 'progress' because it proposes a single interpretation of history such as 'from slavery to feudalism' and 'from feudalism to capitalism'. It is not quite clear whether Marxism aims at employing the interpretation specifically or universally in terms of time and space.

Certainly, Neoclassicism does not *necessarily* assume such notions as 'progress', 'better reform' or 'improvement', though many anti-neoclassicist historians criticise it on the grounds that it does. The agency theory based researchers assume various outcomes across corporations, because they consider agency costs as unique to each company. For example, Watts (1977: 59; see also Watts and Zimmerman, 1979: 277) notes that 'the argument, that a function of audited financial statements in an unregulated economy is to reduce agency costs, could explain which corporations present financial statements and how the contents of those statements vary across corporations'. Another agency theory based researcher, Leftwich (1983: 41) also reveals that 'accounting measurement rules in lending agreements differ systematically from GAAP, the regulated set of accounting rules, because those who

participate in this market for accounting information accept some of the regulated measurement rules, modify others, and design some rules of their own'. From these remarks on the consequences of their theory and analysis, there is no self-evident implication of agency relationships leading to the inevitable single improvement of financial reporting practice. The recent Neoclassicists, however, do not leave their position to implication but make explicit the fact that 'change does not, of course, necessarily mean progress' (Edwards, 1989a: preface).

2.3.3.3 Importance of archival evidence[23]

The last area of the recent Neoclassicism's view outlined in this study is not concerned with methodology but with data collection. The recent Neoclassicism suggests that archival evidence is important for a study of accounting history.

It seems to have been a disputed point among 'traditional' and 'new' accounting historians whether or not archival data should be used by historians. For example, Fleischman and Tyson (2003: 32) describe the 'new' accounting historians' contention that 'primary source material is of limited value because the accounting functions that traditional economic rationalists take for granted (such as striving for efficiency and cost reduction) have "conflictual underpinnings" ... and because of their failure to represent the suppressed voices of the past – the poor, the illiterate, women, the economically powerless for whom accounting records were not an available avenue of expression'. It is also observed that 'practitioners of the new accounting history are loath themselves to get down and dirty in the archives' (Fleischman and Tyson, 2003: 32).

[23] There is a wide variety of relevant evidence for research purposes. Fleischman, Mills and Tyson (1996) demonstrate the kinds of historical evidence, whilst categorising them into the natural, the communicative, and the processive evidence. They consider communicative evidence most important for accounting history, usually taking the form of written documents, such as chronicles, annals, biographies, genealogies, memoirs, diaries, letters, newspapers, literature, public documents, business records, inscriptions.

However, many 'new' historians (for example, Hoskin and Macve, 1986, 1988) have used archival evidence. Even those who did not go to the archives themselves seem to have used the archival findings of others. Walker (2004: 5) described data collection in archives as 'the activity which most distinguishes historians from other researchers in accounting'. Boyns and Edwards (2000: 155) stated their conviction as follows, and it seems agreed today:

> In our view, the preferable route towards theory construction starts with the collection of a range of relevant evidence, an approach which reflects our conviction that historical research method should be driven primarily, though of course not entirely, by an inductivist rather than deductivist approach. (Boyns and Edwards, 2000: 155)

The Rochester school of accounting history seems to have been silent on this matter (Watts and Zimmerman, 1978, 1979) and on this point the recent Neoclassicism can be said to be different from the Neoclassicism surveyed in 2.3.2.

It can be therefore seen that the recent Neoclassicism has expressed its view on three controversial issues discussed above, namely, whether accounting history needs to be located in its broader contexts, whether the notion of 'progress' is appropriate for the study of accounting history, and whether findings and conclusions need to be based on archival evidence. As noted above, the recent Neoclassicism does not provide 'grand theory' of accounting history, but the basic ideas shared by the writers of the school are quite clear as seen above. It can be said that the basic ideas achieve the consensus of the three schools of accounting thought (Neoclassicism, Foucauldianism, Marxism/labour process) and improve the attractiveness of the Neoclassicism. For this reason, this study depends on the approach taken by the recent Neoclassicism.

2.4 Summary

In this chapter, empirical and theoretical studies have been reviewed in order to help locate, within existing knowledge, the current study of the development of group accounting in the UK in the first half of twentieth century.

In the first half of this chapter, prior research on group accounting was surveyed. It was revealed that studies of group accounting embrace an important and difficult issue concerning the purposes/functions of consolidated accounts and the equity method. It was argued that the historical study of group accounting can therefore be justified because 'the examination of past events ... enables us to appreciate the complexity and persistence of many of the problems presently facing accountants' (Edwards, 1989a: 6-7). It was also stated that the rate of accounting change has been well discussed by researchers into the development of group accounting in the UK, but the cause of a lack of change has been paid insufficient attention. In other words, no existing literature has successfully provided a convincing answer to the question: 'Why was the adoption of consolidated accounts slow in the UK?' The latter is the focus of this thesis, which aims at a different and perhaps more persuasive explanation for slow change. For the purpose of providing a more fundamental explanation, it was stated that a theoretical framework is necessary, because a relationship of cause and effect is often difficult to be presented without a conceptual theory.

Seeking for a reasonable theoretical framework for this study, the second half of this chapter surveyed prominent schools of thought, i.e., Neoclassicism, Foucauldianism and Marxism. It was presented that the recent Neoclassicism is most appropriate for the present study, and three basic ideas which distinguish them from the Rochester school of accounting positivists were reviewed. First, accounting history should be understood within its broader contexts (not only economic but also social, cultural and political contexts). Second, the recent Neoclassicism made the point clearly that the notion of 'progress' is inappropriate for

the study of accounting history. Third, unlike the Neoclassicism, the recent Neoclassicism emphasises the importance of archival evidence.

The next chapter will explain why this thesis employs the theory of path dependence as an operating theory for analyzing and interpreting the development of group accounting in the UK in the first half of twentieth century, and how the theory of path dependence can be considered to be consistent with the basic views held by the recent Neoclassicism.

Chapter 3 Methodology

3.1 Introduction

This chapter explains the methodology and theoretical framework employed by this study. As revealed in the previous chapter, this study relies on the conceptual views presented by the recent Neoclassicism in exploring a fundamental answer to the research question. It will be argued that the theory of path dependence is consistent with the recent Neoclassicism's views and also has potential to give a more fundamental explanation for why the adoption of consolidated accounts was slow in the UK.

First, the focus of this study – i.e. the question: 'Why was the adoption of consolidated accounts slow in the UK?' – is introduced again in the form of a visual image of the developmental process, and it will be argued that the research question is related to one aspect of the developmental process, i.e. that which represents no change in group accounting practices in the UK during the first half of twentieth century (section 3.2). In order to explain the absence of change, this study draws on the concept of path dependence. It will be observed that there are divergent definitions concerning the concept of path dependence but its main feature for the purpose of this thesis is that 'history matters' (section 3.3), and it will be explained that this study relies on the evolutionary theory of economics literature to understand path dependence in relation to the concept of 'habits' (section 3.4). Section 3.5 will explain, based on the ideas expressed in the old institutional economics based accounting studies, that habits, i.e. repeated behaviours of individual agents, become institutionalised when shared by groups of agents, and give rise to path dependence and, therefore, resistance to change. The consistency of the theory of path dependence with the basic ideas of recent Neoclassicism will be also discussed.

3.2 The approach of this study

As outlined in chapter 2, the development of group accounting in the UK has not been a straightforward and orderly process. Rather, it has been described as a process which was sometimes changing and was sometimes not changing until the CA48 introduced the legislative requirement for companies to prepare group accounts, normally to consist of a consolidated balance sheet and a consolidated profit and loss account. In other words, the developmental process has two aspects: periods of change and of no change. Indeed, Edwards (1989a: 4) described the development of group accounting in the UK in this light when referring to the existence of factors that encouraged British companies to adopt consolidated accounts and other factors that discouraged change. He also made the point that an explanation for the latter process was not known, whereas the former process was better understood by accounting historians.

> ... we know that consolidated accounts were devised to provide an adequate method for reporting the results of a 'group' of companies. We do not know why the system took so much longer to obtain a foothold in Britain than in, say, the US ... (Edwards, 1989a: 4)

Table 3-1 illustrates the two dimensions of the developmental process, one being movement towards change and the other being lack of change.

Table 3-1 Two dimensions to the development of group accounting in the UK

towards change	*no change*
Garnsey's lecture (1922) Royal Mail case (1931) Dunlop Rubber's accounts (1933) RoAP7 (1944) CA48 (1948)	wide range of group accounting practice (-1933) no provision in CA29 (1929) unpopularity of consolidated accounts in practice (-1945)

Source: original

As stated by Edwards (1989a), and as surveyed in chapter 2, the dimension of accounting practice in the direction of change, culminating in legislation requiring the publication of

consolidated accounts, is well covered in the prior literature compared with the dimension reflecting no change. The five factors that stimulated the use of consolidated accounts by British holding company directors (Garnsey's lecture, Royal Mail case, Dunlop Rubber's accounts, RoAP7 and CA48) are well documented in the previous literature surveyed in sub-section 2.2.2.1. On the other hand, the three issues surrounding the slow adoption of consolidated accounts by British holding companies discovered by previous literature have not been fully explained (sub-sections 1.3.1, 2.2.2.2 and 2.2.2.3). For example, Edwards and Webb (1984) have revealed that companies experimented with a wide range of group accounting methods until 1933 and they enumerated six possible reasons for the phenomenon, but they (p.47) still stated that 'the above is not an exhaustive list of explanations for slow development in the UK'. Kitchen (1972) has traced the process that led the Greene Committee not to recommend the introduction of statutory provisions requiring the publication of consolidated accounts, and Bircher (1988) found unpopularity of consolidated accounts in practice as late as in 1945, but both did not explain why consolidated accounts were slow to be accepted.

In short, factors which militated against group accounting change and resulted in the introduction of legislative requirements as late as 1940s have not been illuminated enough by the preceding literature. It is of course the case that the research question of this study relates to this feature of the history of group accounting. Therefore, in order to provide a fundamental answer to the research question posed in this thesis, this study focuses on the dimension of the process, represented in the right hand column of Table 3-1, which reflects no accounting change.

3.3 The concept of path dependence

Focusing on the process which was characterised by lack of change, this study draws on the concept of path dependence[24] as its theoretical framework. As explained in 2.3.3, this study follows the view held by the recent Neoclassicism. This study selects the concept of path dependence as a possible theory which seems to fit well with the focus of this study, i.e. the process of no change or the mechanism of slow change[25]. The relationship and consistency of the concept of path dependence with the views of recent Neoclassicism will be dealt with later in this chapter.

The concept of path dependence is popular today among social scientists, though at the same time it is claimed that 'clear definitions are rare' (Pierson, 2000a: 252). In this section, the divergent definitions of the path dependence are surveyed at first, and then the viewpoint shared by researchers as the fundamental feature of the concept is introduced. It will be argued that, although it might be true that 'the rising popularity of the term "path dependence" has spawned a variety of usages, a perceptible measure of confusion, and even some outright misinformation' (David, 2001: 15), there is a common understanding on the concept in general. The basic idea of path dependence is that history matters and that the state of the present and the future depends on its own past.

The concept of path dependence was originally introduced in a literature focusing on studies of technological change such as the history of typewriters, electrical currents, railway gauges, video cassette recorders and so on (Cusumamo, et al., 1992; David, 1985, 1987, 1992; Puffert, 2000, 2002; Scott, 2001, 2006). David's papers (David, 1985, 1986) on QWERTY, the topmost row of letters on personal computer keyboard, is said to have achieved the status of 'founding myth of the path dependence literature' (Ruttan, 1997: 1522). David (2001: 19)

[24] Some researchers employ the term 'path dependence' (for example, David, 2001; Arthur, 1994) and some employ the term 'path dependency' (for example, Hodgson, 1993; Ahmed and Scapens, 2000). In this study, the two terms are considered to mean the same idea.

[25] The importance of a theoretical answer to the research question as a (possibly) more persuasive explanation for slow adoption of consolidated accounts in the UK was explained in chapter 2.

defined the concept of path dependence as follows: 'a path dependent stochastic process is one whose asymptotic distribution evolves as a consequence (function of) the process's own history'. The characteristic of his definition is that the concept of path dependence is described by terms from probability theory and physics such as 'stochastic process' and 'asymptotic distribution'.

Other researchers on path dependence have defined the concept in various rather different ways. There seem, roughly speaking, three elements in definitions of path dependence that have been emphasised. First, the strong influence of (possibly accidental and trivial) initial conditions is often referred to (Liebowitz & Margolis, 1995: 206; Arrow, 2000: 175). Second, there is a tendency to focus on the self-reinforcing mechanism of path dependent events (Cowan & Gunby, 1996: 521). It seems that the word 'self-reinforcing' can be rephrased using such terms as 'persistent' (Puffert, 2002), 'stickiness' (Crouch & Farrell, 2004), 'high cost to reverse' (Levi, 1997), and 'persisting' (Scott, 2006). Third, some emphasise the outcome as inefficient and a result of market failure (Liebowitz & Margolis, 1995: 206) or as multiple equilibria (Arthur, 1994; David, 2001).

Thus, it is possible to observe diversity in definitions of the concept of path dependence. However, it seems also possible to say that there is a common understanding of the concept among the researchers. The common feature of path dependence is the notion that 'history matters'. The phrase 'history matters' was introduced by David (1994), in which he attempted to 'establish a common foundation' among the path dependence based researchers. David (1994: 208) stated that 'the expression "history matters" does carry a quite precise set of connotations, namely those associated closely with the concept of path dependence'. In short, the concept of path dependence emphasises the importance of history.

3.4 Path dependence in relation to 'habits'

It has been explained that the concept of path dependence has a connotation of 'history matters'. In this section, a theoretical explanation for why history matters and why path dependence takes place will be provided. In other words, it will be explained that 'history matters' because 'habits' are an important feature of human behaviour. The notion of 'habits' used here refers to the repetitive behaviour of a human agent which is strongly affected by other people. Other people surrounding the agent share a common expectation about how the agent will act, and the agent is expected to follow their expectation. In this context, no matter how rationally an agent thinks and no matter what an agent learns from past, the agent is unlikely to change his/her behaviour radically.

This exercise is important for this thesis in order to apply the concept of path dependence to the analysis of evidence obtained and to provide a theoretically-derived answer to the research question posed in this thesis.

3.4.1 Path dependence as a result of repetitive behaviour

Among many social scientists who have employed the concept of path dependence, this section specifically relies on the discussion of path dependence in the evolutionary theory of economics literature in order to identify how it might help illuminate further the issue of 'history matters'. There is an accounting literature also based on the evolutionary theory of economics and this will be surveyed in the next section in connection to the theoretical framework of this study.

Among the evolutionary theory of economic literature, this study focuses on such works as Hodgson (1993, 1997, 2004) and North (1990, 1999). In his book entitled *Economics and Evolution*, Hodgson introduced several issues under the title of 'towards an

evolutionary theory' (Hodgson, 1993: Part IV) and the phrase 'evolutionary theory of economic literature' is used in this thesis when referring to his work. Path dependence is a central idea of his story, as he believes that 'economics and biology both address complex system, with abundant path dependent developments' (Hodgson, 1993: 266). According to him (Hodgson, 1993: 203), 'the future development of an economic system is affected by the path it has traced out in the past'. Needless to say, this description is consistent to the notion 'history matters' that is shared by many social scientists.

In explaining the concept of path dependence, Hodgson often relates it to the concept of 'habits'. The definition of habit employed by him is: 'a more or less self-actuating disposition or tendency to engage in a previously adopted or acquired form of action' (Camic 1986: 1044).

The concept of habit used here, therefore, is different from the one in ordinary usage. According to *the Oxford English Dictionary*, the most usual current sense of habit is 'a settled disposition or tendency to act in a certain way, especially one acquired by frequent repetition of the same act until it becomes almost or quite involuntary; a settled practice, custom, usage; a customary way or manner of acting'. From this OED's viewpoint of habits, an agent follows habits 'involuntarily' and continuous behaviours happen without intention. In this ordinary usage, a habit is a repeated behaviour without thinking.

On the other hand, habits referred to in the evolutionary economics literature 'have both intentional and causal facets' (Hodgson, 1993: 229). The evolutionary theory of economics literature has thought that, when making a decision under such conditions as complexity or uncertainty, an agent can rely on a habit with intention and deliberation. Unlike the usual meaning, habits in the evolutionary economic context have a characteristic that 'even the most ingrained habits are the objects of recurring mental activity and evaluation' (Hodgson, 1993: 229; see also Hodgson, 2004: 653). This definition of habit is

similar to the concept of rules. Both rules and habits have the form: in circumstances X, action Y follows. Hodgson (1997: 664) states that 'both apply to situations that, in essential terms, are actually or potentially repetitive and non-unique'.

Thus, the concept of path dependence is explained by the evolutionary theory of economics literature as a result of a human agent's tendency to engage in a previously adopted or acquired form of action, that is, habit. Similar attention to repetitive behaviour can be also seen in such works by North (1990, 1999).

North's works (1990, 1999) are also influential among social scientists who adopt the concept of path dependence (Pierson, 2000a: 255; 2000b: 492). North does not use the term 'evolutionary theory' in describing his works but, for the purpose of this study, his works are dealt with in the same way as Hodgson's evolutionary theory, since Hodgson (2004: 655) states that his idea is similar to that of North (1990).

North developed his framework, one which has close parallels with the role of habits as employed by Hodgson, by way of the concept of 'ideas, theories, and ideologies' (North, 1990: 96), 'beliefs or ideologies' (North, 1999: 13-4) and 'shared mental models' (Denzau and North, 1994). North emphasises the importance of those perceptions that a human agent has already obtained in the past. For example, North (1990: 95-6) states that 'if the markets are incomplete ... the historically derived perceptions of the actors shape the choices that they make'.

Accordingly, based on the evolutionary theory of economics, the origin of path dependence is considered to be a repeated and shared behaviour (habits/mental models/beliefs and ideologies). However, this explanation is insufficient for the purpose of this study, because 'habits' are seen as a repeated behaviour of *individual* agents, whereas this study has selected as units of analysis two collective attitudes: (1) British holding company directors' group accounting practices; (2) the British accountancy profession's attitude towards group

accounting. Thus, the next main section will explain how habits of individual agents are interrelated with other people and social system, and become influential in the creation of path dependence.

Before moving on to section 3.5, however, the next sub-section will reveal the similarities and differences between habits and bounded rationality given that both are considered to be important features of human behaviour under the condition of uncertainty. This exercise is necessary because the difference between habits and bounded rationality, for the purpose of this thesis, will be referred to later in this chapter (sub-section 3.5.3).

3.4.2 Relation to the bounded rationality

Traditionally, human behaviour in relation to decision making has been explained by applying the concept of rationality where individuals know what is in their self interest and which choice serves them best[26]. Concerning the conditions of complexity and uncertainty, which the evolutionary theory of economics literature often emphasises, it is relevant to consider the significance of 'bounded rationality' which depicts a human agent's behaviour under such conditions. In this sub-section, the relation of habits to bounded rationality will be surveyed.

The term 'bounded rationality' is defined as 'rational choice that takes into account the cognitive limitations of the decision-maker – limitations of both knowledge and computational capacity' (Simon, 1987: 266). The comparison between rationality and bounded rationality is given as Table 3-2.

[26] Here, the Arrow-Debreu model of general equilibrium is in mind as rational choice under neoclassical settings. For assumptions of Arrow-Debreu model of general equilibrium, see, for example, Geanakoplos, 1987: 116-8.

Table 3-2 The comparison between rationality (neo-classical economics postulates) and bounded rationality postulates

neo-classical economics rationality postulates:	*bounded rationality postulates:*
(1) choices made among a given, fixed set of alternatives;	(1) a process for generating alternatives;
(2) choices made with (subjectively) known probability distributions of outcomes for each;	(2) estimating procedures for probability distributions of outcomes, or dealing with uncertainty that do not assume knowledge of probabilities;
(3) choices made in such a way as to maximize the expected value of a given utility function.	(3) a satisfying strategy

Source: Simon, 1984: 266

Bounded rationality therefore contains characteristics similar to those revealed in the discussion of habits and shared mental models, because both are the antithesis of neo-classical economic rationality given their recognition of uncertainty.

However, according to Hodgson, bounded rationality is different from habits in that habits involve the interaction with others outside. Hodgson (1997: 665) gives the following seven conditions signalling the existence of habits:

1. *Optimisation*: where the choice set is known and it is possible to employ procedures and decision-rules to find an optimum.
2. *Extensiveness*: where the information may be readily accessible and comprehensible but the search for it requires the application of substantial time and other resources.
3. *Complexity*: where there is a gap between the complexity of the decision environment and the analytical and computational capacity of the agent.
4. *Uncertainty*: where crucial information and probabilities in regard to future events are essentially unobtainable.
5. *Cognition*: the general problem of dealing with and interpreting sense data[27].

[27] Concerning 'sense data', Hodgson (1997: 673) explained as follows:

First it is necessary to distinguish between sense data and information. Sense data consist of the multitude of aural, visual and other signals that reach the brain. We have no other contact with the outside world other than through this sense data ... To derive information it is necessary that a prior conceptual framework is imposed on the jumble of neurological stimuli, involving implicit or explicit assumptions, categories or theories which cannot themselves be derived from the sense data alone. Often the sense data

6. *Learning*: the general process of acquiring crucial knowledge about the world.
7. *Communication*: the general need to communicate regularly with others.

(Hodgson, 1997: 665)

According to Hodgson, neoclassical economics, or rational choices under the pure neoclassical theory, completely accommodate *Optimisation*, because it 'requires a fixed, bounded and unambiguous choice set, expressed in terms of certainties or computable probabilities' (Hodgson, 1997: 678). However, rational optimisation does not fully accommodate conditions 2-7.

Behavioural economics, or bounded rationality, has modified the neoclassicism by accommodating conditions 2-4 above (*Extensiveness, Complexity, and Uncertainty*), according to Hodgson. In this sense, bounded rationality is much closer to habits, compared with rational choices. However, bounded rationality is different from habit in that it does not envisage conditions 5-7 (*Cognition, Learning, Communication*) contained in the list above. On the other hand, in the circumstances of 5-7, Hodgson (1997: 664) explained that habits are advantageous in the sense that they help agents to decide, learn and act.

In other words, bounded rationality puts supreme emphasis on the explanation of the behaviour of the single agent and neglects interactions with outside (Langlois, 1986: 236; 1990). In behavioural economics, organisations are considered to be produced because 'it is only because individual human beings are limited in knowledge, foresight, skill, and time that organizations are useful investments for the achievement of human purpose' (Simon, 1957: 199). Thus organisations are a tool for human agents to make up for their limited foresight and skill and to help them achieve their purpose. On the other hand, in evolutionary theory of economics, the possibility is taken into account that the purpose of the agents can be influenced by outside. Communication and learning processes necessarily involve

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are open to different interpretations, as some simple and celebrated optical illusions demonstrate. The attribution of meaning is not direct or automatic. Sense data, unlike the proverbial facts, do not speak for themselves. There has to be a process of cognition, to provide a form that is meaningful and has informational content for the agent. (Hodgson, 1997: 673)

interactions with outside. Thus habit is different from bounded rationality in that the former pays attention to the influence from and upon other people surrounding an agent but that the latter does not.

3.5 Attention to accounting stability

In this section, the process by which a habit of individual agents becomes institutionalised and gives rise to path dependence, as reflected in a collective attitude of a group of people, will be explained by reference to the old institutional economics based accounting literature. By 'the old institutional economics based accounting literature', the present study refers to such works as Ahmed and Scapens (2000), Burns (2000), Burns and Scapens (2000), Scapens (1994), Siti-Nabiha and Scapens (2005). They seem to owe much to the evolutionary economics literature, especially the work of North (Scapens, 1994: 304-13; Ahmed and Scapens, 2000: 168; Burns, 2000: 571; Burns and Scapens, 2000: 13). For example, they refer to North (1990) when they discuss 'path dependence' (Burns and Scapens, 2000: 13), and they also employ Hodgson's idea that routines are formalized or institutionalized habits (Scapens, 1994: 306, 310; Burns, 2000: 571). As explained in sub-section 3.4.1, this thesis regards works by Hodgson and North of equal importance within the evolutionary theory of economic literature, because both pay attention to repetitive behaviour of a human agent.

In this study, the school of accounting thought referred to in the previous paragraph is called 'old institutional economics based accounting literature', rather than 'evolutionary economics based accounting literature', for the following reason. This study employed the term 'evolutionary theory of economics' in order to refer to the works of Hodgson (1993, 1997), because Hodgson himself described the objective of his book as 'towards an evolutionary economics' (Hodgson, 1993: Part IV). However, members of the above school

of accounting thought have described their works using such terms as 'towards an institutional analysis' (Ahmed and Scapens, 2000) and 'an institutional framework' (Burns and Scapens, 2000). In addition, they explained their approach as the application of old institutional economics, mainly to present-day management accounting practices, and their common characteristic is to view management accounting as organizational rules and routines (that is, roughly speaking, institutions). Accordingly, it is considered that they are adequately labelled as 'old institutional economics based accounting literature'. In this sense, the terms 'evolutionary theory' and 'old institutional theory' of economics are used interchangeably in this study.

The works by the old institutional economics based accounting researchers are important for the present study for the following two reasons.

First, they represent research in the field of accounting, though not in accounting history, which is the focus of this study. Also, it must be acknowledged that these researchers' sphere of interest is management accounting rather than the external reporting orientation of the present thesis. However, their theoretical framework is considered useful for this study because, as visualised in Figure 3-2 below, it is concerned with the action of human agents, with interaction with other people, and within the influence of an holistic structure, which are not characteristics confined to studies of management accounting research. The old institutional economics framework is therefore considered to have potential to explain accounting change both inside an organisation (in the case of management accounting) and in the capital market (in the case of financial reporting).

Second, institutional economics based accounting researchers focus on the stability of accounting. For example, the work by Siti-Nabiha and Scapens (2005) is entitled 'Stability and Change: An Institutionalist Study of Management Accounting Change'. In this work they observe that 'accounting change has taken place, but in a reshaped form that does not

threaten the stability of the existing institutions' (Siti-Nabiha and Scapens, 2005: 59; see also Burns and Scapens, 2000: 22). Stability, or events which do not encourage change, is of course the main focus of this thesis[28].

3.5.1 The duality of the process

The old institutional economics based accounting literature informs this study through the provision of a visual image of their theoretical framework which is useful for analysing the development of group accounting in the UK. The framework offers a holistic perspective whereby 'human beings, organizations and the economic system itself are regarded as part of a larger social system' (Ahmed and Scapens, 2000: 167; see also Scapens, 1994: 308). Thus, they consider that 'there is a duality between action (human activity) and the institutions which structure that activity' (Burns and Scapens, 2000: 6)[29].

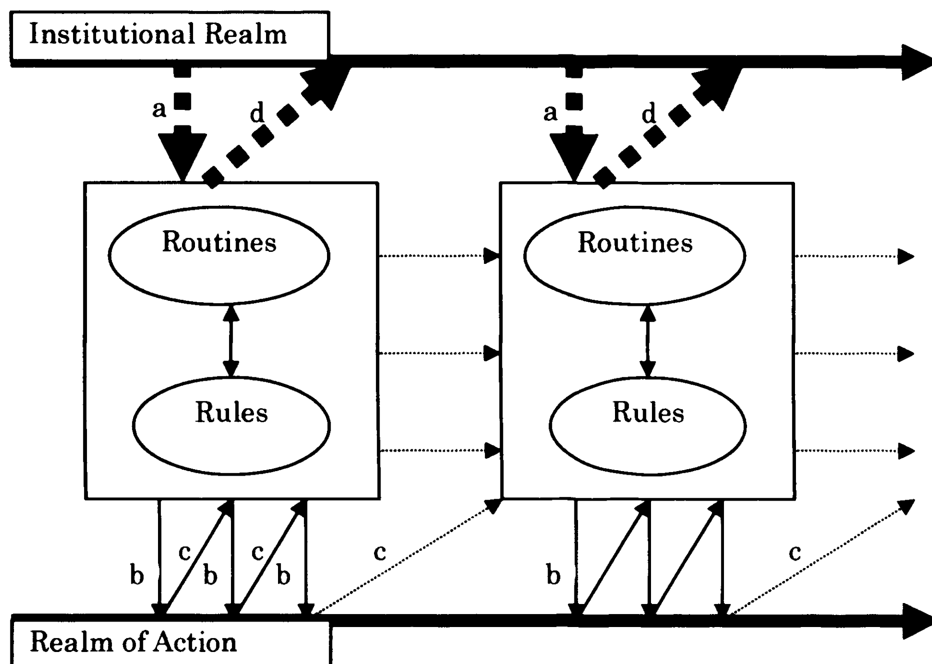
Emphasising the importance of both individual activity and holistic structure, Burns and Scapens (2000: 9) gave a visual image of 'the process of institutionalization' as follows[30].

[28] It is noticed in this study, though the institutional economics based accounting literature does not state clearly, that stability might embrace a different implication from continuity. Both have a similar meaning in that both imply, perhaps in slightly different ways, the lack of change. However, continuity is often used as part of the phrase 'continuity and change', by accounting historians (for example, see Edwards 1996; Littleton and Zimmerman, 1962), and it is reasonable to think that continuity has been usually associated with change. For example, Littleton and Zimmerman stated that 'Continuity in the midst of change has typified the development of accounting' (Littleton and Zimmerman, 1962: 256). Moreover, writers have shown awareness of the fact that change in accounting is not necessarily the normal state of affairs. For example, when Parker (1977a) addressed the issue of the 'causes of changes in accounting practice', he advanced a hypothesis that 'accounting practice only changes as a result of very strong external pressures such as a stock market crash, a major scandal or a major inflation' and at the same time he proposed another hypothesis that 'even then its capacity to change is limited by lack of available accounting theories (or by the unsuitability of existing theories)' (Parker, 1977a: 5). This thesis, consistent with the notion put forward by Parker, understands continuity as a simultaneous event of accounting change, and employs the word of stability in order to refer specifically to events without change.

[29] It can be said that this dual perspective reflects habits' characteristics that became clear in contrast to bounded rationality, that is, interactions with outside. It was mentioned that bounded rationality emphasises the behaviour of the single agent whereas habits take into consideration interactions with outside (3.4.2).

[30] It is noted here that Burns and Scapens (2000: 9) cautioned readers that the framework above was 'not intended to provide operational constructs for empirical research and hypothesis testing'. Rather, they (2000: 9) stated that 'its purpose is to describe and explain analytical concepts which can be used for interpretive case studies of management accounting change'.

Figure 3-1 The Process of Institutionalisation



Key: a=encoding
b=enacting
c=reproduction
d=institutionalisation

Source: Burns and Scapens, 2000: 9

It is clear that Burns and Scapens stress 'duality' and emphasise the importance of the two 'realms', namely the institutional realm shared by group of actors and the realm of action of individual actors. In connection with the concept of path dependence, it can be considered that there are two paths illustrated in Figure 3-2. One is the top bold line which represents a path that an institution traces, and the other is the bottom bold line which represents a path that an individual agent traces. Figure 3-2 explicitly demonstrates that the paths continue over time, which of course can be considered as an image of path dependence.

For the purpose of this study, having selected two collective opinions as units of analysis, that is, (1) British holding company directors' group accounting practices and (2) the British accountancy profession's attitudes towards group accounting, the path in the

institutional realm is more important than that in the realm of action. This is the most important reason for why the old institutional economics based accounting research is dealt with here. The concept of habit discussed by the evolutionary theory of economics literature is related only to behaviour of a single human agent, but Figure 3-2 presents the relationship between individual agents' behaviour and collective behaviour of the group of agents.

3.5.2 The process in which a habit becomes institutionalised

Concerning path dependence as a result of habit, the most important features in Figure 3-2 are the arrows b and c which are repeated in the realm of action. It seems possible to equate the arrows as the concept of habit which was discussed earlier in this chapter, because they represent a repeated behaviour of an individual agent. Figure 3-2 illustrates that the arrows b and c exert their cumulative influence over time on the emergence of rules, routines and consequently the arrow d, which means that the repeated behaviour in the realm of action becomes institutionalised and gives rise to a path in the institutional realm when shared by a group of people. And as can be seen in Figure 3-2, arrows a and d occur less often than arrows b and c, which means that the path in the institutional realm is relatively slower to change. Below, using the old institutional economics based accounting literature, the above process in which a habit becomes institutionalised will be explained.

According to Burns and Scapens (2000: 10), 'the second process (arrow b) involves the actors enacting the routines (and rules) which encode the institutional principles' and 'the third process (arrow c) takes place as repeated behaviour leads to a reproduction of the routines'. Their explanation of the two arrows can be considered to have quite similar features to the concept of habit discussed earlier in this chapter, because both the two arrows and habit refer to an engagement of an individual person with previously adopted or acquired forms of action. Moreover, similar to habit, the arrows b and c are explained as both

reflective and non-reflective behaviour. In Burns and Scapens' (2000: 10) words, the arrow b 'may involve conscious choice, but will more usually result from reflexive monitoring and the application of tacit knowledge about how things are done' and the arrow c 'may involve either conscious or unconscious change'.

One of the two important features of the arrows b and c in Figure 3-2, which can be thus equated to habit for the purpose of this study, is that the arrows are visualized as the reason for the rise of a path in the realm of action. This is, of course, consistent with the concept of path dependence as a result of habit. As Burns and Scapens (2000: 10) put it, 'there is unlikely to be a reopening of previously agreed arrangements and therefore routines may become somewhat resistant to change'.

The other feature of the arrows b and c which is relevant to this study is that they produce and reproduce routines when they are shared within a society or group, and that they may become institutionalised, creating a path not only in the realm of action but also in the institutional realm. The explanations of routines are the same as in the evolutionary theory of economics literature and in the old institutional economics based accounting literature, in that both schools see routines as shared habits by groups of individuals. For example, Burns and Scapens explain routine as follows: 'whereas habits are personal, routines may encompass groups of individuals', and 'routines represent the patterns of thought and action which are habitually adopted by groups of individuals' (Burns and Scapens, 2000: 6; see also Dosi et al., 2000: 5 and Hodgson, 1997: 679). According to the literature, routine in this sense becomes institutionalised when it loses its particular connection to specific actors (for example, Ahmed and Scapens, 2000: 167; Burns and Scapens, 2000: 5-6; Hodgson, 1993). Commenting on Figure 3-2, Burns and Scapens (2000: 10) depict the influence of arrows b and c on the process of institutionalisation as the arrow d, stating as follows:

> The fourth and final process (arrow d) is the institutionalization of rules and routines which have been reproduced through the behaviour of the individual actors. This

> involves a disassociation of the patterns of behaviour from their particular historical circumstances, so that the rules and routines take on a normative and factual quality, which obscures their relationship with the interests of the different actors. In other words, the rules and routines become simply the way things are, i.e., institutions. (Burns and Scapens, 2000: 11)

Thus, the arrows b and c in Figure 3-2, or 'repeated behaviour' (Burns and Scapens, 2000: 10) of individual actors, can be considered to give rise to paths both in the realm of action and in institutional realm. In applying the theory of path dependence, this study will see any repeated behaviour as the central focus which generates the slowness to change, not only for an individual actor but also for a group of people. Specifically, it will be considered that a group accounting method becomes continuously favoured by a group of holding company directors when it is adopted repeatedly and shared by many individual holding companies.

It is noted that, of course, 'institutions *always exist prior to* any attempt by the actors to introduce change, and will therefore shape the processes of change' (Burns and Scapens, 2000: 11) (*emphasis in original*), and that starting the discussion from arrows b and c might be inappropriate for the old institutional economics based researchers. In other words, it might be more desirable to focus on 'arrow a' at first. However, for the purpose of this thesis, the attention to repeated behaviour is necessary to discuss the concept of path dependence as a result of habits, and arrows b and c are paid much more attention than the arrow a.

3.5.3 Relevance of the concept for the study

Thus, it seems reasonable for this study to rely on the theory of path dependence, as a result of habits, when focusing on the dimension of the developmental process of group accounting in the UK which showed no change (Figure 3-1). This is because the habits of individual actors become institutionalised, over time, when shared by a group of people who, as a result, become slow to change their opinions and actions. In this sub-section, it will be stated that

the theory of path dependence is consistent with the three viewpoints that the recent Neoclassicism, whose methodology this study follows, has expressed. The recent Neoclassicism has made clear the importance of sensitively locating accounting history within its appropriate broader contexts, of resisting temptations to make value judgments about whether or not accounting has progressed and of ensuring that findings are based on sound evidence (see sub-section 2.3.3 in chapter 2).

First, as the comparison with bounded rationality (sub-section 3.4.2) revealed, the theory of path dependence as a result of habits pays much attention to the outside environment. It was stated that the bounded rationality puts supreme emphasis on the explanation of the behaviour of the single agent, while path dependence recognises that the actions of the agents can be influenced by outsiders. Similarly, in Figure 3-2, arrow b was explained to be an enacting process of the institutional principles. The above explanation of the aspect of the theory of path dependence seems to suggest that the theory is conscious of an influence of social and cultural elements surrounding the human agent. In this connection, the concept of path dependence as a result of habits can be said to be consistent with the recent Neoclassicists' view that not only economic but also social and cultural contexts should be taken into consideration. In this connection, it is interesting to note here that Boyns and Edwards (1996: 47) made the point that the different development *paths* in different settings are reflecting the different socio-economic contexts.

> ... we believe that historians need to be aware of the possibility that accounting may have followed different development *paths* in different countries, otherwise they may be led mistakenly to view development in different countries as being part of a single process when, in fact, there may have been different processes reflecting the different socio-economic contexts prevailing in each country. (Boyns and Edwards, 1996: 47) (*emphasis added*)

Second, the concept of path dependence can be seen to be consistent with the view of recent Neoclassicism, because both reject the concept of 'progress'. As seen above, the theoretical

framework of path dependence emphasises repeated behaviour and influence of the past, rather than behaviour aiming at improvement and higher achievement. It is also the case that the emphasis is on differences between paths rather than the superiority of one over another. For example, Denzau and North (1994: 3-4) state that 'individuals with different learning experiences (both cultural and environmental) will have different theories (models, ideologies) to interpret their environment' (Denzau and North, 1994: 3-4). An examination of the content of Figure 3-2 reveals arrows which might be taken to imply progress of some sort, but Burns and Scapens (2000) do not characterise the arrows as progress. The arrows can of course be argued as signalling progress from the standpoint of the people inside a company (or other organisation), in the sense that they usually act to achieve an aim or target and, when they get closer to the aim or target, it is natural for them to think that they have made progress. However, from Burns and Scapens' point of view, the arrows signify time, not progress, because the intention behind the figure is 'to describe and explain analytical concepts which can be used for interpretive case studies of management accounting change' (Burns and Scapens, 2000: 9). Moreover, there is no sign that they engage with the notion of progress. The disregard of the notion of progress in their framework is consistent with the avoidance of value judgement by the recent Neoclassicism.

Recognition of reliance on previously acquired behaviour in solving problems can also be seen in Boyns and Edwards' following statement:

> Our research suggests that British businessmen, in certain quarters, have always been aware of the problems they faced and have attempted to find solutions to such problems by adapting existing accounting practices rather than developing wholly new ones. (Boyns and Edwards, 1997: 42)

Thus, the theory of path dependence and the views expressed by the recent Neoclassicists are similar in that both emphasise paths which are sustained over time and both avoid value judgments about whether one path is more advanced than another.

The third point is not an issue concerning the theory of path dependence itself, but concerning the present study and how to use the theory. The recent Neoclassicism sees archival evidence as the dominant force in the study of accounting history. In other words, they emphasise archival evidence-based research rather than theory-driven research. Therefore, consistent with this approach, this study emphasises archival evidence. This is an archival-informed thesis which applies the theory of path dependence. In other words, this study employs the research method of (1) collecting evidence from archival sources and (2) making some tentative conclusions based on the evidence, and (3) examining the conclusions if there can be any elements that are consistent with the concept of path dependence. This is not a theory-driven research, because it does not look for evidence which supports the concept of path dependence. By employing the research method, it is considered both possible to follow the recent Neoclassicism and to seek a theoretical explanation to the slow adoption of consolidated accounts in the UK.

3.6 Summary

In this chapter, the methodology and the conceptual framework used in this thesis has been explained. In order to illuminate the lack of change in the developmental process of group accounting in the UK, the theory of path dependence was selected. It was explained that the notion that 'history matters' is central to the concept of path dependence, and that, consistent with the evolutionary economics literature, history matters because 'habits' are an important feature of human behaviour. The relationship between the concept of path dependence and bounded rationality was also considered. Grounded on the old institutional economics based accounting studies, 'habits' of individual agents are considered to become institutionalised over time when shared by a group of people and, as a result, become resistant to change.

It was explained that this study's methodology, depending on the theory of path dependence, is consistent with three viewpoints expressed by recent Neoclassicism in the following ways (for the three viewpoints, see sub-section 2.3.3 of chapter 2). First, the concept of path dependence encourages this study to be sensitive to the complex interrelationships between human agents and social institutions. Second, the concept does not assume the notion of 'progress' in accounting history. As the third point, it was stated that this thesis emphasises on archival evidence. This is an archival-informed thesis which applies the theory of path dependence, which is consistent with the recent Neoclassicism's approach in that emphasise is on the importance of conducting evidence-based research, rather than theory-driven research.

Chapter 4 Group Accounting Practices 1927-1950: Findings

4.1 Introduction

The purpose of this chapter is to track group accounting practices adopted by British companies between 1927 and 1950, with particular emphasis placed on use of the equity method of accounting. Using 1,545 sets of accounts published by British holding companies, obtained from a dataset of 2,943 sets of accounts, this chapter reveals three main facts. First, it shows that group accounting was adopted by more companies in later years than in earlier years. Second, among the six methods of group accounting (the definition of six methods is given in section 4.4 of this chapter), publication of consolidated accounts together with legal entity-based accounts (method 6) became increasingly popular, particularly after RoAP7 and CA48 each took effect. Third, it is shown that a fairly constant percentage of holding companies adopted the equity method, the most popular method in the early years, throughout the period investigated.

While the publication of consolidated accounts can be easily observed because in most cases holding company directors present the accounts in a manner which clearly indicates whether they are consolidated or combined, the adoption of the equity method is not always entirely straightforward. The level of adoption of the equity accounting is important to establish, however, given the concern of this thesis with slowness of change based on the theoretical framework described in chapter 3. Therefore, the main focus of this chapter is dedicated to an examination of the use of the equity method by British holding company directors, carefully explaining which cases can be considered to be the equity method for the purpose of this study.

The next two sections will explain the periods and companies investigated in this study. The periods selected for the purpose of this study are 1927/28, 1930/31, 1942/43, 1946/47 and 1950/51. Companies' accounts published in those accounting years will be examined in this

chapter. Section 4.4 presents the findings from the investigation of company accounts between 1927 and 1950, and this section comprises the main part of the chapter. Section 4.5 presents a summary. The findings will be analysed and interpreted in chapter 5.

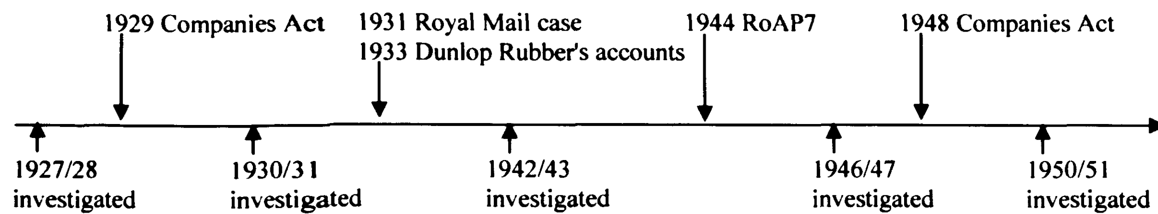
4.2 Periods investigated

The accounting periods investigated for the purpose of this study were 1927/28[31], 1930/31[32], 1942/43[33], 1946/47[34] and 1950/51[35]. The choice of dates may be explained as follows. The company annual reports filed in 1927/28 and in 1930/31 reflect, respectively, group accounting practice before and after the CA29 took effect[36]. As stated in chapter 2, the CA29 required holding companies to state how the profits and losses of subsidiaries had been dealt with in the accounts of the holding company. The years 1927/28 and 1930/31 are used to see the effect of the requirement on group accounting practices. The accounts published in 1942/43 are used to examine practice after the effects of the Royal Mail case and the 'trail-blazing' accounts of the Dunlop Rubber company should have become fully apparent, but before the RoAP7 took effect. Similarly, the 1946/47 accounts would reflect the practice after RoAP7 and before the CA48 took effect[37], and the accounts of 1950/51 the practice after the relevant provisions of CA48 became statutory requirements. The RoAP7 provided

[31] In 1927/28, the selected companies' financial year ended between 30 September 1927 and 31 August 1928.
[32] In 1930/31, the selected companies' financial year ended between 27 July 1930 and 31 August 1931.
[33] In 1942/43, the selected companies' financial year ended between 30 September 1942 and 31 July 1943.
[34] In 1946/47, the selected companies' financial year ended between 30 September 1946 and 31 July 1947.
[35] In 1950/51, the selected companies' financial year ended between 30 June 1950 and 31 August 1951.
[36] The CA29 took effect from 7th February 1929 (except that Section 92 came into operation only from 1st November 1929) (*The Statutory Rules & Orders and Statutory Instruments Revised to December 31, 1948*, Volume IV, 1950: 738).
[37] The CA48 took general effect from 1st July 1948 (some Sections including the Section 18, which provides the meaning of 'holding company' and 'subsidiary', came into operation from 1st December 1947, 'so far as applicable to Sections 42 to 49 inclusive of the Companies Act, 1947, and Sections 135 to 138 inclusive of the Companies Act, 1929') (*The Statutory Rules & Orders and Statutory Instruments Revised to December 31, 1948*, Volume IV, 1950: 739-40). Some companies adopted the Act earlier with the accounts filed for 1947/48 already prepared in compliance with CA48.

encouragement and CA48 introduced a legal requirement for holding companies to publish group accounts, with the preferred form being consolidated accounts. Table 4-1 illustrates this historical sequencing of events.

Table 4-1 Key events and periods investigated in this study



Source: original

4.3 Companies investigated

Among the preceding literature, de Paula (1948) and Edwards (1991) are case studies of individual companies, Dunlop Rubber Co. and Pearson & Knowles Coal and Iron Co., respectively. Edwards and Webb (1984), Bircher (1988) and Arnold and Matthews (2002) explored collective data from companies' accounts. In this study, the company data gathered are collective as well, because Dunlop Rubber Co. and Pearson & Knowles Coal and Iron Co. are single company studies while the sample numbers of Bircher (1988) and Arnold and Matthews (2002) are relatively small; 40 companies for Bircher (1988) and 50 for Arnold and Matthews (2002). It therefore seems appropriate to extend the data set to provide the basis for a broader and fuller analysis of accounting practices.

The collection from which the study sample has been selected – the sets of published accounts filed with the London Stock Exchange and now located at the Guildhall Library, Corporation of London – represents a first class archive for the purpose of this investigation.

As revealed below, the selection of companies is not appropriate in a statistical sense because it does not follow the technique of random sampling. The reason for selecting the data in the manner chosen is because company accounts are stored at Guildhall Library by industrial sector and in alphabetical order. If the sample was identified at random, it would make this investigation impractical given restrictions placed by the Guildhall library on the number of files that can be consulted on any one day. Therefore it must be acknowledged that the companies data investigated cannot be used validly for statistical estimation. The analysis in the next chapter will be preceded on the basis of descriptive statistics.

The sample sets of accounts, used for this study are taken from two industrial categories and compiled in the following manner.

First, all Iron, Coal & Steel companies (IC&S companies) and the Commercial & Industrial companies (those companies whose names start with A, B, C and D) (C&I companies) listed in the Stock Exchange Year Books[38] of 1926, 1933, 1942, 1946 were selected. For 1950/51, the companies whose names start with A and B provided a comparable-sized sample.

Second, from amongst these companies were identified those where information about their auditors, their issued capitals and the stock exchanges on which they were listed are all given for analysis purposes[39]. This produced: 223 IC&S companies and 308 C&I companies for 1927/28; 188 IC&S companies and 333 C&I companies for 1930/31; 183 IC&S companies and 381 C&I companies for 1942/43; 197 IC&S companies and 407 C&I companies for 1946/47; and 184 IC&S companies and 539 C&I companies for 1950/51.

From these sets, companies are classified as holding companies for the purpose of this study where one or more of the following listed conditions are satisfied:

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[38] Stock Exchange Year Books of 1926, 1933 and 1952 were used instead of 1927, 1930 and 1950 because the latter were unavailable to the author, and Stock Exchange Year Books of 1926, 1933 and 1952 were the closest to 1927, 1930 and 1950 among the available Year Books to the author.

[39] There are some companies who lack all three types of information, mainly because of being founded abroad.

For 1927/28,

- any type of group accounts is submitted;
- the legal entity-based balance sheet identifies the existence of a 'subsidiary' or 'associated company' through entries such as 'shares in subsidiary (associated company)' and 'loans to subsidiary (associated company)';
- the legal entity-based balance sheet itemizes 'shares in the other companies'[40];
- the legal entity-based balance sheet shows name(s) of other company(ies)[41] among the list of assets[42].

For 1930/31, 1942/43, 1946/47,

- any type of group accounts is submitted;
- the legal entity-based balance sheet identifies the existence of a 'subsidiary' through entries such as 'shares in subsidiary' and 'loans to subsidiary'[43];

---

[40] It cannot be known for certain whether 'the other companies' are subsidiaries or not. However, the reasons of selecting those companies as holding companies in this study are the following. First, in 1927/28, the term 'subsidiary' was not uniformally adopted. Some companies use the term 'associated company' and some companies specify the names of subsidiaries. Second, in the 1920s assets are only classified in balance sheets, often in very broad terms, and it is not unusual to find some companies listing assets under only a couple of headings. Under these circumstances, the relatively specific item of 'shares in the other companies' makes it clear that the investment has different characteristics from investments such as government securities. Third, at the time of the Greene Committee, a witness (the London Chamber of Commerce) used the term '*investments in other companies* which are subsidiary to or associated with the Company in question' (cited in Walker, 1978: 65) (*emphasis added*). Therefore it seems plausible to infer that 'shares in the other companies' is an abbreviation of 'shares in the other companies which are subsidiary to or associated with the company'. It might also be worth making the point that this period of time is considered to be 'a time when the subsidiaries of holding companies were usually wholly-owned or nearly wholly-owned' (Walker, 1978: 280).

[41] Banks at which cash was held were naturally excluded.

[42] It is, of course, unknown if the companies whose names are shown in balance sheets are subsidiaries or not. However, there are cases where holding company accounts show a company's name and add the company's profit to the holding company's profit. In this study the treatment is classified as the equity method. For example, see the accounts of The British Automatic Company Limited, dated at 30th September, 1927, which will be reproduced later.

[43] CA29 defined the term 'subsidiary' for legal purposes (Section 127).

- the legal entity-based balance sheet is accompanied by a statement from the directors in compliance with Section 126 of CA29 concerning how a subsidiary has been accounted for[44].

For 1950/51,

- any type of group accounts is submitted;
- the legal entity-based balance sheet identifies the existence of a 'subsidiary' through entries such as 'shares in subsidiary' and 'loans to subsidiary';
- the legal entity-based balance sheet is accompanied by a statement from the directors in compliance with Section 15(4) of the Eighth Schedule to the CA48 concerning why no group accounts are submitted.

For all years, the mere appearance of the item 'investment' in the balance sheet does not result in an entity being treated as a holding company due to the inability to attach any particular significance, in terms of the level of share ownership, to that label. Also, where subsidiaries have not been trading during the year or where holding company's directors state that all subsidiaries' accounts were not available for them (usually the explanation is that they were operating abroad), the holding company is excluded from the sample.

Table 4-2 reveals that the published accounts of 168 companies in 1927/28, 264 companies in 1930/31, 323 companies in 1942/43, 364 companies for 1946/47 and 426 companies for 1950/51 contained data suitable for the purpose of this study.

[44] CA29 required the statement 'signed by the persons by whom in pursuance of Section 129 of this Act the balance sheet is signed, stating how the profits and losses of the subsidiary company, or where there are two or more subsidiary companies, the aggregate profits and losses of those companies, have, so far as they concern the holding company, been dealt with in, or for the purposes of, the accounts of the holding company' (Section 126).

Table 4-2 Holding companies investigated

	Iron, Coal & Steel			*Commercial & Industrial*			*examined*
	all cos	*cos judged to be holding cos (a)*		*A-, B-, C-, & D- cos**	*cos judged to be holding cos (b)*		*holding cos (a+b)*
1927/28	223	81	36.3%	308	87	28.2%	168
1930/31	188	96	51.1%	333	168	50.5%	264
1942/43	183	100	54.6%	381	223	58.5%	323
1946/47	197	111	56.3%	407	253	62.2%	364
1950/51	184	91	49.5%	539	335	62.2%	426

* A- and B- companies for 1950/51

Source: derived from an analysis of company accounts

4.4 Findings

This study recognises and distinguishes between six methods of group accounting. This categorization is based on previous literature (Edwards and Webb, 1984), except for modification of the definition of method 1[45].

method 1: The inclusion of profits and losses of subsidiary companies in the holding company's statutory (legal entity-based) accounts irrespective of dividends actually declared or paid.

method 2: Balance sheets of subsidiaries published in addition to the holding company's statutory accounts.

method 3: Combined statement of assets and liabilities of subsidiaries published in addition to the holding company's statutory accounts.

method 4: Combined statement of assets and liabilities of group published in addition to the holding company's statutory accounts

method 5: Consolidated balance sheet published instead of the holding company's statutory

[45] Edwards & Webb (1984) describe method 1 as 'Profits earned by subsidiaries accounted for on the accruals basis in the holding company's statutory accounts', but this has been changed as above since the original definition cannot handle cases where subsidiary companies incur losses.

accounts

method 6: Consolidated balance sheet published in addition to the holding company's statutory accounts.

Companies have been judged to be users of the equity method where any one of the following Conditions is satisfied.

Condition 1. Profits are exactly the same amount in legal entity-based accounts and in consolidated accounts;

Condition 2. There is a clear statement that profits of subsidiary companies in holding company's legal entity-based accounts are 'undistributed' or 'accrued' profits[46];

Condition 3. For the years of 1927/28, it is possible to deduce from the wording used that profits and losses of the subsidiary companies have been included in the legal entity-based profit and loss account;

Condition 4. For the years of 1930/31, 1942/43 and 1946/47, a statement from the directors in compliance with Section 126 of CA29 explains that profits and losses of the subsidiary companies have been included in the legal entity-based accounts;

Condition 5. For the year of 1950/51, a statement from the directors in compliance with Section 15(4) of the Eighth Schedule to the CA48 explains that profits and losses of the subsidiary companies have been included in the legal entity-based accounts.

It is acknowledged that quite often the full amount, rather than a proportionate amount, of losses incurred by subsidiary companies was provided for by the holding company[47].

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[46] A well-known example of this type is the published accounts of Lever Brothers, Limited for the year ended on 31 December 1925. It is a common understanding among accounting historians that the company employed the equity method at the time.

[47] For example, Dicksee stated as follows:

Table 4-3 shows the number and proportion of holding companies which were judged to be employing group accounting methods 1-6.

Table 4-3 Companies employing group accounting methods 1-6

	companies employing group accounts								*companies not employing group accounts*	*sample holding cos******
	method 1	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*other***	*total**		
1927/28	7	1	2			3		13	156	168
	4.2%	0.6%	1.2%	0.0%	0.0%	1.8%		7.7%	92.9%	100.0%
1930/31	36	3	2	1	2	9		53	215	264
	13.6%	1.1%	0.8%	0.4%	0.8%	3.4%		20.1%	81.4%	100.0%
1942/43	41	9	1	1	1	41		94	242	323
	12.7%	2.8%	0.3%	0.3%	0.3%	12.7%		29.1%	74.9%	100.0%
1946/47	49	8	3	1	2	127		190	204	364
	13.5%	2.2%	0.8%	0.3%	0.5%	34.9%		52.2%	56.0%	100.0%
1950/51	34	16	1		2	371	4	428	29	426
	8.0%	3.8%	0.2%		0.5%	87.1%	0.9%	100.5%	6.8%	100.0%

* The total presented in this column may be greater than that of the number of firms employing group accounting methods due to double counting of companies which used a combination of methods. This was the case for 1 company in 1927/28 (adopting 1&6), 4 companies in 1930/31 (1 company adopting 1&2 and 3 companies adopting 1&6), 13 companies in 1942/43 (1 company adopting 1&2, 1 company adopting 1&4, 11 companies adopting 1&6), 30 companies in 1946/47 (1 company adopting 1&3, 28 companies adopting 1&6, 1 company adopting 2&6) and 31 companies in 1950/51 (29 companies adopting 1&6, 1 company adopting 2&3, 1 company adopting 2&6).

** other 1950/51 2&3&6 1 company
parent B/S + consolidated P/L 2 companies
new type 1 company

*** Due to double counting (see note * above), the sample of holding companies is not the sum of the previous two columns

Source: original

4.4.1 Finding 1 – Group accounting growing in number

The first finding is that group accounting is employed more in later years than in earlier years. The percentage of companies engaging with group accounting among the holding companies examined grows from 7.7% in 1927/28 to 20.1% in 1930/31, to 29.1% in 1942/43, to 52.2%

It is quite correct that its proportion of profits, only, should be taken up, but in many cases a holding company owning, say, ninety per cent. of the stock of another company, which is being operated by it in connection with other companies, should take up all the loss of the latter rather than its proportion only, which in this case would be ninety per cent. (Dicksee, 1924: 293)

in 1946/47 and to 100.5% in 1950/51[48].

It is also noticeable that publishing subsidiary companies' balance sheets (method 2), publishing combined accounts of subsidiary companies (method 3), publishing combined accounts of the group without consolidation procedures (method 4) and publishing consolidated accounts without holding company's individual accounts (method 5) have been the relatively less popular methods throughout the entire study period.

4.4.2 Finding 2 – Rate of adoption of consolidated accounts

The second finding is that presenting consolidated accounts together with legal entity-based accounts (method 6) has become increasingly popular, particularly in the periods of 1946/47 and 1950/51, that is, after RoAP7 and CA48 each took effect. Consolidated accounts are used by 1.8% companies in 1927/28, 3.4% in 1930/31, 12.7% in 1942/43, 34.9% in 1947/48, and 87.1% in 1950/51.

4.4.3 Finding 3 – Relative popularity of the equity method

Finding 3 (derived from Table 4-3) is that the equity method (method 1) was most used by British holding companies until 1942/43 and a fairly constant percentage of holding companies still employed the method in 1946/47.

We now turn to a detailed examination of the adoption of equity accounting in each of the five periods selected for study. As mentioned in the Introduction (section 4.1) to this chapter, the adoption of the equity method is more difficult to observe than the employment of consolidated accounts. This is mainly because consolidated accounts were usually clearly identified as consolidated, combined or amalgamated accounts, whereas there was no common name for the group accounting practice recognised today as the equity method or its

[48] The reason why more than 100% of holding companies appear to employ group accounting methods in 1950/51 is that 31 companies are counted twice because they adopt two methods at the same time, while 29 companies adopted no method of group accounting.

historical variation as defined for use in this study. The rest of this chapter is dedicated to the presentation of evidence concerning the use of the equity method by British holding company directors. This is because its continued use is a central focus of this study in order to answer the research question.

4.4.3.1 Evidence for 1927/28

In the accounting year of 1927/28, seven British holding companies contained in the data set for this study are judged to be using the equity method (Table 4-3). Table 4-4 is a list of names of the companies. One company (Crosse & Blackwell) satisfied Conditions 1 and 2, one company (H. H. and S. Budgett and Company) satisfied Condition 2 and five companies satisfied Condition 3.

Table 4-4 Companies adopting the equity method 1927/28

	Company	*Industry**	*Consolidated B/S*	*Condition***
1	Amalgamated Anthracite Collieries	ICS	No	3
2	Babcock and Wilcox	ICS	No	3
3	Bournemouth Imperial and Grand Hotels	CI	No	3
4	British Automatic Company	CI	No	3
5	British Oxygen Company	CI	No	3
6	Budgett (H.H. and S.) and Company	CI	No	2
7	Crosse & Blackwell	CI	Yes	1+2

* ICS for Iron, Coal & Steel industry; CI for Commercial & Industrial
** the Conditions introduced in 4.4
Source: original

Below are reproduced illustrative examples taken from the published accounts demonstrating the adoption of the equity method through compliance with Conditions 1-3.

Figure 4-1 is an extract from annual reports of Crosse & Blackwell, Limited. The company is the only one that satisfied the Condition 1, i.e. profits are exactly the same

amount in legal entity-based accounts and in consolidated accounts. The company's 'Amalgamated Profit & Loss Account', 'Balance Sheet' and 'Amalgamated Balance Sheet' are reproduced below for illustrative purposes. The company did not publish its legal entity-based profit and loss account. The balances of 'Profit and Loss Account' in the balance sheet and in the amalgamated balance sheet show the same amount (£136,114 8 6). This indicates that the Condition 1 is satisfied. Moreover, on the assets side of the balance sheet, there is an item worded 'Advances to Subsidiary Companies and *Profits not yet transferred*' (*emphasis added*). This proves that the company satisfies also the Condition 2 (There is a clear statement that profits of subsidiary companies included in holding company's legal entity-based accounts are 'undistributed' or 'accrued' profits).

Figure 4-1 Crosse & Blackwell, 1927/28

Crosse & Blackwell, Limited and Subsidiary Companies

Amalgamated Profit & Loss Account ended 31st December, 1927

	£	s.	d.		£	s.	d.
To Head Office Directors' Fees and Remuneration, Office and Travelling Expense, Legal Charges, Expenses of Annual Meeting, &c., for Year to 31st December, 1927	31,995	4	11	By Trading Profits for the year	207,253	18	6
" Interest Paid	1,204	15	1				
" Proportion of Note Issue Expenses written off	3,681	1	3				
" Balance, being Profit for the year	170,372	17	3				
	£207,253	18	6		£207,253	18	6

Crosse & Blackwell, Limited

Balance Sheet, 31st December, 1927

	£	s.	d.		£	s.	d.
To SHARE CAPITAL	2,728,981	12	0	By FEEHOLD PROPERTIES- *Less* Depreciation	5,991	13	6
" LOANS WITH INTEREST ACCRUED	737,774	17	8	" PLANT, MACHINERY AND OFFICE FURNITURE- *Less* Depreciation	167	7	4
" SUNDRY CREDITORS AND CREDIT BALANCES	5,661	4	10	" STOCK IN TRANSIT	1,141	14	5
" RESERVE ACCOUNT	55,073	15	5	" SUNDRY DEBTORS AND PAYMENTS IN ADVANCE	12,026	11	8
" PROFIT AND LOSS ACCOUNT Balance brought forward 31st December, 1926 50,116 11 3				" SHARES IN SUBSIDIARY COMPANIES (uncalled liability £3,061)-	2,680,451	19	9
Profit for the year ended 31st December, 1927, as per Amalgamated Account annexed 170,372 17 3				" ADVANCES TO SUBSIDIARY COMPANIES AND PROFITS not yeat transferred	926,568	19	7
220,489 8 6				" CASH AT BANKERS AND IN HAND	8,186	3	0
Less-				" PREMIUM AND EXPENSES NOTE ISSUE	17,242	17	6
Dividend on First Preference Shares to 30th June, 1927				" EXPENSES CAPITAL REORGANISATION	2,828	11	8
84,375 0 0	136,114	8	6		£3,663,605	18	5
	£3,663,605	18	5				

Crosse & Blackwell, Limited and Subsidiary Companies

Amalgamated Balance Sheet, 31st December, 1927

	£	s.	d.		£	s.	d.
CAPITAL ISSUED (excluding Inter-Company Holdings)-	2,728,981	12	0	FREEHOLD AND LEASEHOLD PROPERTIES	1,207,635	19	5
Shares in Subsidiary Companies not held by Crosse & Blackwell, Limited	232,468	8	4	MACHINERY, PLANT, LOOSE TOOLS, UTENSILS, FURNITURE AND FITTINGS	450,036	11	6
				MOTORS, VANS AND HORSES	25,109	6	10
LIABILITIES	1,444,883	1	5	STOCK	801,081	15	4
RESERVE FUND	55,073	15	5	DEBTORS AND BILLS RECEIVABLE	411,671	7	0
PROFIT AND LOSS ACCOUNT	136,114	8	6	LOANS	4,350	0	0
				CASH AT BANKERS, IN HAND AND IN TRANSIT	22,595	3	9
				PATENTS IN ADVANCE	137,492	1	10
				INVESTMENTS AND ADVANCES	27,868	13	4
				PREMIUMS PAID ON MORTGAGE REDEMPTION POLICY	4,892	8	8
				GOODWILL, TRADE MARKS, &c.	1,450,000	0	0
				DEVELOPMENT ACCOUNT	34,716	8	10
				PREMIUM AND EXPENSES NOTE ISSUE	17,242	17	6
				EXPENSES CAPITAL REORGANISATION	2,828	11	8
	£4,597,521	5	8		£4,597,521	5	8

Source: Annual Report of Crosse & Blackwell, Limited, 31st December, 1927.

The Condition 2 is also satisfied by H. H. and S. Budgett & Co., Limited. Figure 4-2 is an extract from the annual reports of the company. The company did not publish consolidated

accounts, which makes it impossible to test for compliance with the Condition 1. However, as shown in Figure 4-2, its 'Revenue Account' contains 'Net Profit on Trading to 29th February, 1928, after deducting Taxation Liabilities and including a Credit in respect of *accrued Profits in Associated Companies*' (*emphasis added*).

Figure 4-2 Budgett (H. H.&S.) & Co., 1927/28

H.H. & S. Budgett & Co., Limited

Revenue Account ending February 29th, 1928

	£	s.	d.		£	s.	d.
To Interim Dividend on Preference Shares at the rate of 7.5 per cent. per annum for the half-year ended 30th September, 1927 (less Income Tax)	10,799	19	9	By Balance brought forward from the year ended 28th February, 1927, per Directors' Report of 28th June, 1927	6,256	9	3
" Sundry Charges for the year ended 29th February, 1928, Interest, Bonus Fund, Trade Subscriptions, Donations, and Sundry Reserves	6,414	10	8	" Net Profit on Trading to 29th February, 1928, after deducting Taxation Liabilities and including a Credit in respect of accrued Profits in Associated Companies	7,518	7	2
" Balance Carried forward, 29th February 1928	19,386	0	10	" Interest Account	2,797	6	4
				" Transfer Fees	28	8	6
				" Reserve Fund- Amount Transferred	20,000	0	0
	£36,600	11	3		£36,600	11	3

H.H. & S. Budgett & Co., Limited

Balance Sheet, February 29th, 1928

	£	s.	d.		£	s.	d.
Capital Issued and Fully Paid	410,000	0	0	Goodwill as at formation of the Company on 21st July, 1898	35,445	3	10
Sundry Creditors and Bills payable	133,659	14	1	Premises, Plant, Machinery, &c.	81,463	13	1
Loans and Deposits	94,864	11	8	Debtors on Sales Ledger Accounts	105,247	16	11
Reserves	26,586	2	3	Debtors on Bought Ledger, Stock and other Accounts	20,151	11	4
Reserve Fund	20,000	0	0	Bank and Cash Accounts	38,091	4	9
Revenue Account- Balance 29th February, 1928	19,386	0	10	Stock-in-Trade on hand	88,464	7	9
				Stock in Transit	11,208	14	4
				Investments, -including holdings in and Loans to Associated Companies	324,423	16	10
	£704,496	8	10		£704,496	8	10

Source: Annual Report of H.H. & S. Budgett & Co., Limited, 29th February, 1928.

Figure 4-3 contains extracts from the annual reports of five companies which have been judged as users of the equity method because all of them refer to the inclusion of profits from

subsidiary or other companies[49] (the Condition 3 is satisfied). It must be noted that the wording of Babcock & Wilcox, Limited, is ambiguous, referring to income (which might mean profits *or* dividends).

Figure 4-3 Other companies, 1927/28

Amalgamated Anthracite Collieries, Limited

Profit and Loss Account ended 31st December, 1927

	£	s.	d.		£	s.	d.
To Balances of Interest *less* Dividends received	4,607	8	1	By Trading Profits of the Subsidiary Companies of Amalgamated Anthracite Collieries, Limited, for the year ended 30th June, 1927, *less* trading loss of the Amalgamated Company and Subsidiary company for the six months ended 31st December, 1927	21,811	15	9
" Interest on Debentures of New Rhos Anthracite Collieries, Limited	1,442	9	6	" Transfer and Resigtration Fees	294	17	0
" Audit Fees	1,275	0	0				
" Directors Fees	6,025	0	0				
" Balance carried to Balance Sheet	7,856	15	2				
	£22,106	12	9		£22,106	12	9

Babcock & Wilcox Limited

Profit & Loss Account ending 31st December, 1927

	£	s.	d.		£	s.	d.
To Rents, Rates, Taxes, Insurance, and Repairs and Alternations to Offices	19,362	4	7	By Manufacturing Profit, less amount written off- for Depreciation, Managing Director's Remuneration, Secretary and Chief Accountant's Salary and Office Salaries, Bad and Doubtful Debts, Travelling, and General Expenses at home and abroad, but including income from Associated Companies	767,698	16	2
" Patents Expenses and Fees	2,251	7	9	" Interest on Investments, Deposits, and Dividends on Shares	156,327	6	10
" Directors' and Auditors' Remuneration and Accountants' Charges	7,424	2	6	" Discount and Interest	21,474	0	6
" Reserve for Income Tax	173,118	9	2	" Transfer Fees	476	10	0
" Balance Profit for the year ending 31st December, 1927, carried to Balance Sheet	743,820	9	6				
	£945,976	13	6		£945,976	13	6

The Bournemouth Imperial and Grand Hotels, Limited

Profit and Loss Account ended 30th, June 1928

	£	s.	d.		£	s.	d.
To Income Tax	900	6	6	By Net Profits from Imperial and Grand Hotels	13,089	16	9
" Directors' and Auditors' Fees and Managing Director's Commission	1,909	11	8	" Net Rents, Interest received, etc.	491	16	1
" Balance carried to Balance Sheet	10,774	9	8	Transfer Fees	2	15	0
	£13,584	7	10		£13,584	7	10

[49] Amalgamated Anthracite Collieries, Limited, uses the term 'subsidiary company', while Babcock & Wilcox Limited calls it 'associated company'. The Bournemouth Imperial and Grand Hotels Limited, the British Automatic Co., and the British Oxygen Company Limited publish names of companies (Imperial and Grand Hotels, Limited, Automatic Machine Business and Reeves, Limited, and Oxygen Limited) whose profits are included. As mentioned in footnote 42, those companies whose names are shown in accounts of 1927/28 and whose profits are absorbed are considered as subsidiaries.

The British Automatic Company Limited

Profit and Loss Account to 30th September, 1927

	£ s. d.		£ s. d.
To Rents of Offices, Rates, Insurance and Income Tax	6,114 2 10	By Profits arising from the Automatic Machine Business and Reeves, Limited, and interest on Investments and Miscellaneous Receipts	82,949 7 1
" General Expenses, Including Staff Travelling, Depreciation on Office Fittings, and other incidentals	4,842 15 3		
" Tobacco Licences	831 6 9		
" Postages and Stationery	1,766 13 11		
" Law Expenses and Stamp Duty	252 16 10		
" Renewal Fees on Patents	19 10 6		
" Auditors' Fees	210 0 0		
" Directors' Fees	1,800 0 0		
" Balance, being net profit for the year	67,112 1 0		
	£82,949 7 1		£82,949 7 1

The British Oxygen Company Limited

Profit and Loss Account ended 31st March 1928

	£ s. d.		£ s. d.
To Trustees' Remuneration	105 0 0	By Balance of Profits at Head Office and Branches, including that of Oxygen Limited, and after deducting Depreciation, Bonus to Staff and Remuneration to the Managing Director and Assistant Managing Director	133,105 18 3
" Directors' Remuneration	2,850 0 0	" Interest and Dividends	18,764 14 5
" Amount set aside under the Trust Deed for interest on, and redemption of, Debenture Stock	23,500 0 0	" Transfer Fees	72 11 0
" Balance of Profit carried to Balance Sheet	125,488 3 8		
	£151,943 3 8		£151,943 3 8

Sources: Annual Reports of Amalgamated Anthracite Collieries, 31 December 1927; Babcock & Wilcox, 31 December 1927; the Bournemouth Imperial and Grand Hotels, Limited, 30th June 1928; the British Automatic Co., 30 September 1927; the British Oxygen Company Limited, 31st March 1928.

4.4.3.2 Evidence for 1930/31

In the accounting year of 1930/31, thirty-six British holding companies are judged to be using the equity method in the data set for this study (Table 4-3). Table 4-5 is a list of names of the companies. 27 companies are judged as users of the equity method solely through compliance with Condition 4, i.e. the content of the directors' statement in compliance with Section 126 of CA29, and two solely through compliance with Condition 1. Six companies satisfied Conditions 2 and 4 and one company each of Conditions 1, 2 and 4.

Table 4-5 Companies adopting the equity method 1930/31

	Company	*Industry**	*Consolidated B/S*	*Condition***
1	Aberdeen Lime Company	CI	No	4
2	Aeolian Company	CI	Yes	1
3	Albion Motor Car Company	CI	No	4
4	Angus (George) & Company	CI	No	4
5	Ardath Tobacco Company	CI	No	4
6	Associated Dyers & Cleaners	CI	No	4
7	Baird (Hugh) and Sons	CI	No	4
8	Baker (Charles) and Company	CI	No	4
9	Bleachers' Association	CI	No	2+4
10	Borax Consolidated	CI	No	4
11	Bovis	CI	No	4
12	Bradford Dyers' Association	CI	No	4
13	Brazilian Warrant Company	CI	No	4
14	British Cotton and Wool Dyers Association	CI	No	4
15	British Cyanides Company	CI	No	4
16	British Glues and Chemicals	CI	No	4
17	British Oil and Cake Mills	CI	No	2+4
18	Budgett (H.H. & S.) and Company	CI	No	2+4
19	Cammell Laird and Company	ICS	No	4
20	Campbells and Stewart & McDonald	CI	No	4
21	Card Clothing & Belting	CI	No	4
22	Cawthra (J.) and Company	CI	No	4
23	Components	CI	No	4
24	Cooper, McDougall & Robertson	CI	No	2+4
25	Copestake, Crampton & Company	CI	No	4
26	Crosfield (Joseph) and Sons	CI	No	2+4
27	Crosse & Blackwell	CI	Yes	1+2+4
28	Crosses & Winkworth Consolidated Mills	CI	No	4
29	De La Rue (Thomas) and Company	CI	No	2+4
30	Dick (W.B.) and Company	CI	No	4
31	Duck, Son & Pinker	CI	No	4
32	Ebbw Vale Steel, Iron and Coal	ICS	Yes	1
33	Grayson, Rollo & Clover Docks	ICS	No	4
34	Manchester Collieries	ICS	No	4
35	Smith, Parkinson & Cole	ICS	No	4
36	United National Collieries	ICS	No	4

* ICS for Iron, Coal & Steel industry; CI for Commercial & Industrial
** the Conditions introduced in 4.4
Source: original

There are 9 companies which published both consolidated accounts and legal entity-based accounts in 1930/31 (Table 4-3). Of these companies, 3 have the same profits/losses in both sets of accounts, while 6 companies show different amounts. The three companies (Aeolian, Crosse & Blackwell, and Ebbw Vale Steel, Iron and Coal) are considered to satisfy Condition 1 and judged to be users of the equity method.

The accounts of Crosse & Blackwell published for the year of 1930/31 are not considerably different from the accounts in 1927/28 which were reproduced as Figure 4-1 in this chapter. Extracts from the accounts published by Aeolian are reproduced below as Figure 4-4. It must be admitted that, for 1930/31, the presence of Condition 1 does not provide such unassailable evidence of use of the equity method as was the case in 1927/28. This is because, as Figure 4-4 indicates, the accounts of company are reporting losses both in consolidated accounts and in legal entity-based accounts. By 1930/31, it was rather common practice to provide for subsidiary companies' losses in the parent's accounts, even if the holding company is adopting the cost method[50] rather than the equity method, in valuing shares in subsidiary companies. That is, we cannot be certain that these companies would have accrued fully the results of the subsidiaries if they had generated a profit rather than a loss. However, the company is picked up through an automatic scrutinising of the data set, because its balances of profit and loss account in consolidated accounts and legal entity-based accounts are the same amount (Condition 1 nevertheless remains satisfied).

[50] The 'cost method' involves 'cost-based asset valuation and dividend-based revenue recognition' (Walker, 1978a: 6). In other words, under the cost method, the investment in subsidiary companies is presented at cost, and only the amount of dividend paid by the subsidiary companies are recognised as revenue of the holding company.

Figure 4-4 Aeolian, 1930/31

The Aeolian Company, Limited

Balance Sheet, 30th June 1931

	£	s.	d.		£	s.	d.
To Share Capital	430,000	0	0	By Bond Street Property	255,000	0	0
" Mortgage Debentures	325,000	0	0	" Freehold Property at Hayes	285,871	1	5
" Bank Loan	73,500	0	0	" Leasehold Properties and Improvements	3,015	10	0
" Mortgage on Bond Street Property	100,000	0	0	" Furniture, Fixtures and Fittings	21,998	1	2
" Aeolian Co., New York	317,806	10	0	" Investments in Subsidiary Companies	5,523	2	4
" Indebtedness to Subsidiary Companies	2,712	2	7	" Amount due by Aeolian Weber Piano			
" Sundry Trade Creditors and Accrued Charges	40,459	4	2	and Pianola Company New York	25,879	9	10
" Preference Dividend	7,031	5	0	" Trade Investments	1,500	0	0
" Reserve Accounts	155,758	15	4	" Mortgage Redemption Policy	5,141	13	4
				" Stock of Manufactured Goods,			
				Raw Materials, Work in Progress, &c.	81,122	0	2
				" Sundry Debtors	163,918	16	4
				" Payments in Advance	615	17	7
				" Bills Receivable	15,474	1	8
				" Cash at Bank and in Hand	20,657	0	4
				" Trade Marks and Patens	1	0	0
				" Profit and Loss Account	241,550	2	11
	1,127,267	17	1		1,127,267	17	1

Profit & Loss Account for the Year ended 30th June, 1931

	£	s.	d.		£	s.	d.
To Net Deficiency on Trading and Reorganisation	115,615	9	0	By Dividends from Investments	883	9	9
" Debenture and Mortgage Interest	9,791	8	9	" Transfer Fees	11	7	6
				" Deficiency Carried to Balance Sheet	124,422	0	6
	125,316	17	9		125,316	17	9

The Aeolian Company, Limited, and of the Companies of which it is sole proprietor

Amalgamated Statement of the Assets and Liabilities at 30th June 1931

	£	s.	d.		£	s.	d.
To Share Capital	430,000	0	0	By Bond Street Property	255,000	0	0
" Mortgage Debentures	325,000	0	0	" Freehold Property at Hayes	285,871	1	5
" Bank Loan	73,500	0	0	" Leasehold Properties and Improvements	3,015	10	0
" Mortgage on Bond Street Property	100,000	0	0	" Furniture, Fixtures and Fittings	21,998	2	2
" Aeolian Co. New York	317,806	10	0	" Amount due by Aeolian Weber Piano			
" Sundry Trade Creditors and Accrued				and Pianola Company New York	25,879	9	10
Charges	40,482	3	4	" Trade Investment	21,278	6	10
" Preference Dividend	7,031	5	0	" Mortgage Redemption Policy	5,141	13	4
" Reserve Accounts	175,280	15	11	" Stock of Manufactured Goods, Raw			
				Materials, Work in Progress, &c.	82,821	16	10
				" Sundry Debtors	164,414	16	5
				" Payments in Advance	615	17	7
				" Bills Receivable	15,688	14	1
				" Cash at Bank and in Hand	20,822	2	10
				" Trade Marks and Patens	3	0	0
				" Profit and Loss Account	241,550	2	11
	1,144,100	14	3		1,144,100	14	3

Source: Annual Reports of the Aeolian Company, 30th June, 1931.

There are seven companies in 1930/31 which satisfy Condition 2 (see Table 4-5). One is Crosse & Blackwell, which also meets Condition 1. The accounts of H. H. & S. Budgett published for the year of 1930/31 are not considerably different from the accounts in 1927/28 which was reproduced as Figure 4-2 in this chapter. The accounts of Bleachers' Association

(Figure 4-5), British Oil and Cake Mills (Figure 4-6), Cooper, McDougall & Robertson (Figure 4-7), Crosfield (Joseph) and Sons (Figure 4-8) and De La Rue (Thomas) and Company will be examined respectively.

Figure 4-5 is an extract from annual reports of Bleachers' Association. The company explains the figure of 'shares in subsidiary companies' as 'being the excess of the Assets over the Liabilities of such companies'. It seems plausible to assume that the amount 'the assets over the liabilities of subsidiary companies' includes undistributed profits of subsidiaries. It is considered in this study that this case satisfies the Condition 2, even though the company does not use the words 'undistributed' or 'accrued' profits of subsidiary companies.

Figure 4-5 Bleachers' Association, 1930/31

Extract from list of assets in balance sheet at 31 March 1931
Shares in Subsidiary Companies being the excess of the Assets over the Liabilities of such Companies, as shown by their Books (including Goodwill and Trade Marks assigned to such Companies) also fully paid Shares in Companies whose businesses have been acquired by purchase of the Shares

£744,212/9/5d

Source: Annual Reports of Bleachers' Association, 31st March, 1931.

Figure 4-6 is an extract from annual reports of the British Oil and Cake Mills, Limited. The company discloses the treatment of its subsidiary's undistributed profits both in the balance sheet and in the profit and loss accounts. In the balance sheet, investments in subsidiary companies are valued by 'Shares (taken at Cost) and balance of *Undistributed* Profits less provisions for ... ' In the profit and loss account, it is clearly stated that '*undistributed* profits less provision for losses of subsidiary companies' are credited (*emphasis added*).

Figure 4-6 British Oil and Cake Mills, 1930/31

Extract from list of assets in balance sheet at 31 December 1930
Investments in and Indebtedness of Subsidiary Companies Shares (taken at Cost) and balance of Undistributed Profits less provisions for Losses

£1,818,126/2/6d

Extract from explanation of revenue in profit and loss account at 31 December 1930
Balance of trading account, after Crediting dividends receivable from and undistributed profits less provision for losses of subsidiary companies and dividends on investments and after adjustment of Reserves for Taxation and Contingencies and crediting Reserves no longer required

£248,963/4/5d

Source: Annual Reports of the British Oil and Cake Mills, 31st December, 1930.

In the cases of Cooper, McDougall & Robertson (Figure 4-7) and Crosfield (Joseph) & Sons (Figure 4-8), the inclusion of subsidiary's undistributed profit is revealed in their Profit and Loss Accounts.

Figure 4-7 Cooper, McDougall & Robertson, 1930/31

Extract from explanation of revenue in profit and loss account at 30 September 1930
Profit on Trading, including undistributed profits of Subsidiary Companies less losses, for the year to 30th September, 1930, and after charging Directors' salaries and fixed remuneration for services

£238,097/5/5d

Source: Annual Report of Cooper, McDougall & Robertson, 30th September, 1930.

Figure 4-8 Crosfield (Joseph) and Sons, 1930/31

Extract from explanation of revenue in profit and loss account at 31 December 1930
Profit for the 13 months ended 31st December, 1930, after charging Repairs, Depreciation, Insurance, Advertising, and all expenses and including Dividends estimated to be received on Investments and the Company's proportion of the undistributed profits less losses of Subsidiary and Allied Companies, partly estimated

£598,458/9/4d

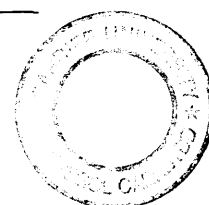
Source: Annual Reports of Crosfield (Joseph) & Sons, 31st December, 1930.

Within the last case that satisfies Condition 2 is that of De La Rue (Thomas) and Company. In this case, the treatment of including undistributed profits of subsidiary companies cannot be seen in published accounts, but in the 'statement required by Companies Act, 1929, Section 126' which states that 'The Profits and Losses of Subsidiary Companies have been brought into account *irrespective of dividends* declared by such subsidiaries' (*emphasis added*). It is clearly inferred by this statement that the company uses the equity method.

Table 4-6 is a list of directors' statements in compliance with Section 126 of CA29 of the nine companies satisfying Conditions 1 and 2. It can be observed that all of them simultaneously satisfy Condition 4, i.e. there is a Section 126 statement that indicates inclusion of profits and losses of subsidiary companies.

Table 4-6 Directors' statements indicating adoption of the equity method, 1930/31

	Company	*Section 126 statement*
1	Aeolian Company	The losses of the Subsidiary Companies have been carried forward in their own accounts, but have been provided for in the above account.
2	Bleachers' Association	The Profits and Losses of all the Subsidiary Companies have been included in the Accounts of the Association.
3	British Oil and Cake Mills	The above Profit and Loss Account includes all Dividends receivable from Subsidiary Companies in respect of the year ended 31st December, 1930, and the balance of their Undistributed Profits as at that date. Any losses have been provided for in the Accounts of this Company.
4	Budgett (H.H.&S.) and Company	The profits of Subsidiary Companies have been brought to Credit in the above Profit and Loss Account, and full provision made therein for any losses sustained by Subsidiary Companies.
5	Cooper, McDougall & Robertson	The Company's proportion of the undistributed profits and losses of Subsidiary Companies have been credited and debited respectively in the Profit and Loss Account.
6	Crosfield (Joseph) and Sons	The above figure of profit has been arrived at after crediting and debiting respectively the Company's proportion of the total profits and losses, partly estimated, of Subsidiary Companies for the 13 months ended 31st December 1930.



7	Crosse & Blackwell	This Company's proportion of Profits and Losses of Subsidiary and Associated Companies is included in the above Profits with the exception of Losses in connection with Canadian and French Factories.
8	De La Rue (Thomas) and Company	The Profits and Losses of Subsidiary Companies have been brought into account irrespective of dividends declared by such Subsidiaries.
9	Ebbw Vale Steel, Iron and Coal	The aggregate losses made by the four Subsidiary Companies have been dealt with in this Company's Profit and Loss Account.

Source: Annual Reports 1930/31.

Table 4-7 is a list of other companies and their directors' statements in compliance with Section 126 of CA 29. It can be reasonably assumed from the statements that the companies are users of the equity method (Condition 4 is satisfied). In the case of holding companies having plural subsidiary companies and treating their profits and losses in different ways, the main treatment was examined to decide whether it includes results of subsidiary companies. When there is no indication among the plurality of treatments which is the main treatment, the first mentioned treatment is assumed to be the main treatment for the purpose of this study.

The archives reveal that there are two main types of wordings used in the Section 126 statements made by directors.

1. the profits and losses of the subsidiary companies have been included in the accounts of the company
2. the profits and losses of the subsidiary companies have been included in the accounts of the company *to the extent of dividends declared*

It is assumed that wordings corresponding to 1 above indicate use of the equity method. It is of course possible that the term profit is used in a loose manner and does not properly describe inclusion of the holding companies' entire share of the profit of a subsidiary. However, this is impossible to confirm and the interpretation adopted is reasonable.

Table 4-7 Companies indicating inclusion of subsidiary companies' profits and losses, 1930/31

	Company	*Section 126 statement*
1	Aberdeen Lime Company	The Profits and Losses made by Subsidiary Companies have been included in the Profit and Loss Account.
2	Albion Motor Car Company	The profits for the year include the profits earned by the Subsidiary Company for the year ended 30th September, 1930.
3	Angus (George) & Company	A loss has been incurred by a Subsidiary Company during the last year for which its accounts are available, and so far as such loss relates to shares held by this Company it has been provided for by writing down the book value of Investments held by this Company in Subsidiary Companies. The profit earned by a Subsidiary Company for the past year has been taken credit for in the accounts of your Company.
4	Ardath Tobacco Company	The profits made by subsidiary companies for the year ended 30th June, 1931, have been included in the above account.
5	Associated Dyers & Cleaners	Associated Dyers & Cleaners Limited owns the whole of the Issued Capitals of all its Subsidiaries. All the Subsidiaries carried profits for the year ended 31st December, 1930, and those profits are included in the above Profit and Loss Account.
6	Baird (Hugh) and Sons	The Profit from the Subsidiary Company has been included in the above figures.
7	Baker (Charles) and Company	The Profit of the Company for the year ended 31st January, 1931, includes the Profit of the Subsidiary Company for the same period.
8	Borax Consolidated	The Profits or Losses shown in the Accounts of Subsidiary Companies made up to a date within the year ended 30th September, 1930, have been dealt with, in arriving at the figure of profit shown in the annexed Profit and Loss Account, as follows:- The profits of two Subsidiary Companies earned, during the year, have been, as hitherto, included in the profits of Borax Consolidated, Ltd. The profits made by four other Subsidiary Companies, during the year, have not yet been distributed by those Subsidiaries, but Borax Consolidated, Ltd., has received, as hitherto, dividends declared by these Companies out of profits made in previous years. The profit made by one Subsidiary Company has been retained by that Company and used to write down losses made in previous years.
9	Bovis	Profits earned by Subsidiary Companies for the period covered by the last audited accounts have been merged in those of the Company and no losses have been incurred by such Companies.
10	Bradford Dyers' Association	The profits and losses of all subsidiary companies have been included in the accounts of this company.
11	Brazilian Warrant Company	The aggregate profits and losses of the Subsidiary Companies for the year ended 31st December, 1930, have been taken into the

		accounts of the Brazilian Warrant Agency and Finance Company Limited, with the exception of the Cia. Unial dos Transportes, in respect of which the dividend paid on shares held by this Company has been taken in, and of Cmmbuby Coffee and Cotton Estates Ltd., the accounts of which Company showed a loss for the year ended 31st December, 1930, which has been carried forward, no part of which has been provided for in these accounts.
12	British Cotton and Wool Dyers Association	The Profits and Losses of the Subsidiary Companies are included in the Association's Profit and Loss Account as Profits and Losses of the Association except in the case of one Company from which Dividends have been received and these are also included in the profits of the Association.
13	British Cyanides Company	The Profits and Losses of all the Subsidiary Companies for the year ended 30th June, 1931, have been included in or provided for out of the profits of this Company. In the case of Beatl Sales, Ltd., the Auditors' Report is qualified as follows: 'Subject to the capitalization of Expenditure on Advertising and Developments, £3,238 1*s*. 5*d*. during the year ended 30th June, 1931, making a total of £8,194 11*s*. 8*d*., to that date.'
14	British Glues and Chemicals	The Company's proportions of profits and losses of its subsidiary companies as disclosed by their accounts made up during the year is brought to credit of, or reserved for in, the above Profit and Loss Account.
15	Cammell Laird and Company	The Profit shewn by the Subsidiary Company (Tranmere Bay Development Co. Ltd.) for the year ended December 31st, 1930, which represents an adjustment of the Rental Charge amounting to £16 4s. 4d., is included in the above Profit and Loss Account.
16	Campbells and Stewart & McDonald	The results of the Export Company's operations are embodied in the above figures.
17	Card Clothing & Belting	In compliance with the Companies Act, 1929, the Directors inform the Shareholders that the results for the year as shown by the Profit and Loss Accounts of the Subsidiary Companies have been embodied in this Company's Profit and Loss Account.
18	Cawthra (J.) and Company	The assets and liabilities and trading transactions of one Subsidiary Company are incorporated in the Accounts of the Parent Company. No part of the profits of the other Subsidiary Company is included in the foregoing Profit and Loss Account.
19	Components	The trading results of Ariel Works Ltd., are merged in the accounts of the Parent Company. Provision has been made for the loss of a subsidiary company and credit has been taken for dividend declared by another Subsidiary Company.
20	Copestake, Crampton & Company	The result of the trading of Copestake, Crampton & Co. (Colonial) Limited is included in the Profit and Loss Account, the whole of the Capital of the Company having been provided by Copestake, Crampton & Co., Ltd.
21	Crosfield (Joseph) and Sons	The above figure of profit has been arrived at after crediting and debiting respectively the Company's proportion of the total profits and losses, partly estimated.
22	Crosses & Winkworth	The aggregate Profits and Losses of Subsidiary Companies to the

	Consolidated Mills	date of this Balance Sheet, so far as they concern this Company, have been credited or fully provided for, as the case may be, in the foregoing Balance Sheet, except the Profits and Losses of Crosses & Heatons' Associated Mills, Limited. Which are shown in the Balance Sheet of that Company annexed to this Account. The amount of Working Capital advanced to the Subsidiary Companies is included in the Assets and Liabilities.
23	Dick (W.B.) and Company	With regard to this Company's Subsidiary Companies: 1. The profits of W. B. Dick & Company, Inc., for the year 1930 have been included in the above Balance Sheet. 2. The profits of two other Subsidiary Companies for the year 1930 have not been included in the above Balance Sheet. 3. The remaining Subsidiary Company has sustained a loss for the year 1930. No provision has been made in the above Balance Sheet for such loss, as it is more than covered by the Reserve standing in the Books of the Subsidiary Company itself.
24	Duck, Son & Pinker	The Profits of the Subsidiary Company for the period covered by this account have been incorporated with those of the Parent Company.
25	Grayson, Rollo & Clover Docks	The Profits and Losses of Subsidiary Companies have been included in the above Accounts.
26	Manchester Collieries	The above Profit and Loss Account includes the Profits of the Company's Subsidiaries for the year to 31st March, 1931.
27	Smith, Parkinson & Cole	The Profits and Losses of all Subsidiary Companies have been included in the Accounts of this Company, and the Trade Creditors and Debts of the Subsidiary Companies as at 31st March, 1931, have been incorporated in the above Balance Sheet.
28	United National Collieries	It is hereby declared that the profit of Subsidiary Company, Burnyeat, Brown & Co., Limited, has been set against accumulated losses in that Company's Balance Sheet. Credit for the profit has been taken in the above Balance Sheet.

Source: Annual Reports 1930/31.

4.4.3.3 Evidence for 1942/43

In the accounting year of 1942/43, 41 British holding companies are judged to be using the equity method in the data set for this study (Table 4-3). Table 4-8 is a list of names of the companies. 14 companies satisfied either Condition 1 or Condition 2, and 10 of them satisfied simultaneously Condition 4. These examples are considered to present rather strong evidence of using the equity method. The other 4 companies satisfied only Condition 1, whose reason will be stated below. The remaining 27 companies are judged as users of

the equity method by examining Condition 4, i.e. their directors' statement in compliance with Section 126 of CA29. Sufficient examples of these treatments are given in the previous part of the thesis and no further illustrations are provided here.

Table 4-8 Companies adopting the equity method 1942/43

	Company	*Industry**	*Consolidated B/S*	*Condition***
1	Adams (Thomas)	CI	No	4
2	Albion Motors	CI	No	4
3	Allen (Edgar) & Co.	ICS	No	4
4	Allen (J. J.)	CI	No	4
5	Amalgamated Anthracite Collieries	ICS	Yes	1+2+4
6	Angus (George) & Company	CI	No	4
7	Ardath Tobacco Company	CI	No	4
8	Associated British Maltsters	CI	Yes	1+2+4
9	Associated Coal & Wharf Companies	ICS	Yes	1
10	Barrow, Hepburn and Gale	CI	Yes	1+4
11	Barton & Sons	CI	Yes	1
12	Bedford (John) & Sons	ICS	No	4
13	Bleachers' Association	CI	No	2+4
14	Bradford Dyers' Association	CI	No	2+4
15	British Cotton and Wool Dyers Association	CI	No	4
16	British Glues and Chemicals***	CI	Yes	1
17	British Quarrying Company	CI	No	4
18	Brockhouse (J.) & Co.	CI	Yes	4
19	Brookes (W. J.) & Sons	CI	No	4
20	Broom and Wade	CI	No	4
21	Brown (David) & Sons (Huddersfield)	CI	No	4
22	Burberrys	CI	No	4
23	Bulter (William) & Co. (Bristol)	CI	No	4
24	Campbells and Stewart & McDonald	CI	No	4
25	Cannock Associated Collieries	ICS	Yes	1
26	Clay (Henry) and Bock & Company	CI	No	4
27	Cooper, McDougal & Robertson	CI	No	2+4
28	Copestake, Crampton & Company	CI	No	4
29	Crosfield (Joseph) and Sons	CI	No	2+4
30	Crosfields Oil and Cake Company	CI	No	4
31	Crosse & Blackwell	CI	Yes	1+2+4
32	Crosses and Winkworth Consolidated Mills	CI	No	4
33	Dent, Allcroft & Co.	CI	No	4
34	Devas, Routledge and Company	CI	No	4
35	Doulton & Co.	CI	No	4
36	Federated Foundries	ICS	Yes	1+2+4
37	Robinson (Thomas) and Son	ICS	No	4
38	Sanderson Brothers and Newbould	ICS	No	4
39	Smith, Parkinson & Cole	ICS	No	4
40	Stephenson (Robert) & Hawthorns	ICS	No	4
41	United Steel Companies	ICS	Yes	1+4

* ICS for Iron, Coal & Steel industry; CI for Commercial & Industrial
** the Conditions introduced in 4.4
*** no Section 126 statement was found.
Source: original

There are 41 companies which published both consolidated accounts and legal entity-based accounts in 1942/43 (Table 4-3). Out of these companies, 10 companies have the same profits in the two sets of accounts (Condition 1 was satisfied), while 31 companies show different amounts[51]. One company (J. Brockhouse & Co.) presents different profits, but the directors' Section 126 statement reveals that the reason of the difference is an exceptional treatment of a part of profits made by subsidiary companies[52].

Figure 4-9 is an extract from Amalgamated Anthracite Collieries, which gives concrete evidence of using the equity method. The company satisfies Conditions 1, because the same amount of profit (£36,521) is shown both in consolidated and legal entity-based balance sheets. The company also satisfies Condition 2, because it reveals that 'Shares in Subsidiary Companies' is including the undistributed profits. Finally, the company satisfies Condition 4, because it states that profits and losses of subsidiary companies are included in their accounts.

[51] All of the ten companies show their accumulated profits. Therefore, unlike the two cases in 1930/31, the ten companies in 1942/43 which have the same profit amounts both in consolidated accounts and in legal entity-based accounts do not require any doubt about their use of the equity method. However, attention needs to be paid to four companies which satisfy only Condition 1. Within the ten companies satisfying Condition 1, as shown in Table 4-8, six companies simultaneously satisfy Condition 4 (and Condition 2). These six examples are considered to provide relatively strong evidence that indicates the use of the equity method. On the other hand, the four companies do not provide such strong evidence. This is because three of them actually adopt the cost method, rather than the equity method, since their Section 126 statements reveal that they include Subsidiary companies' profits only to the extent of dividends paid. It is possible for cost method users to show the same profits both in consolidated and in legal entity-based accounts, as long as the dividends are paid just the same amount of their proportion in subsidiary profits. One company (British Glues and Chemicals) does not provide strong evidence either, because their Section 126 statement was not found and it is impossible to know whether they used the equity method or the cost method.

[52] 'The Profits of Subsidiary Companies have been included in the above Profit and Loss Account except the sum of £819 11s. 6d. Three Subsidiary Companies have shown losses which have been provided as above.'

Figure 4-9 Amalgamated Anthracite Collieries, 1942/43

Amalgamated Anthracite Collieries Limited
Balance Sheet, 31st December 1942

	£	£		£	£
Capital		4,186,770	Collieries and Other Properties and Plant and Machinery		4,769,370
Surplus and Reserves			Shares in Subsidiary Companies, at Directors' Valuation, 1st July, 1938, with additions at cost, together with the undistributed profits		1,855,181
Reserve for Depreciation of Group Plant and Machinery	440,000				
Profit and Loss Account	36,521				
		476,521			
Debenture Stock and Advances from Bankers		1,934,552	Current Assets		861,336
Current Liabilities and Provision		888,044			
		£7,485,887			£7,485,887

Amalgamated Anthracite Collieries Limited
Consolidated Balance Sheet at 31st December 1942

	£	£		£	£
Capital		4,186,770	Fixed Assets		5,557,552
Surplus and Reserves			Semi-Fixed Assets		516,235
Reserve for Depreciation of Group Plant and Machinery	440,000		Current Assets		1,770,338
Profit and Loss Account	36,521				
		476,521			
Debenture Stock and Advances from Bankers		2,060,558			
Current Liabilities and Provision		1,120,266			
		£7,844,115			£7,844,115

126 statement
Profits and Losses of Subsidiary Companies have been taken to credit or provided for in the above accounts.

Source: Annual Report of Amalgamated Anthracite Collieries Limited, 31st December 1942.

4.4.3.4 Evidence for 1946/47

In the accounting year of 1946/47, 49 British holding companies are judged to be using the equity method in the data set for this study (Table 4-3). Table 4-9 is a list of names of the companies. The selection of the companies was conducted in the same way as in the 1930/31 and 1942/43. Sufficient examples of these treatments are given in the previous part of this chapter and no further illustrations are provided here.

Table 4-9 Companies adopting the equity method 1946/47

	Company	*Industry**	*Consolidated B/S*	*Condition***
1	Adams (Thomas)	CI	No	4
2	Aerated Bread Company	CI	Yes	1
3	Albion Motors	CI	No	4

4	Allen (Edgar) & Co.	ICS	No	4
5	Allen (J. J.)	CI	No	4
6	Allied Produce Company	CI	Yes	2+4
7	Amalgamated Anthracite Collieries	ICS	Yes	1+4
8	Amalgamated Cotton Mills Trust	CI	Yes	1+2+4
9	Angus (George) & Company	CI	No	4
10	Associated British Maltsters	CI	Yes	1+2+4
11	Associated Piano Company	CI	Yes	1+4
12	Associated Provincial Picture Houses	CI	Yes	1+4
13	Barrow, Hepburn and Gale	CI	Yes	1+4
14	Bedford (John) & Sons	CI	No	4
15	Birmingham Small Arms Company	CI	Yes	1+4
16	Blantyre and East Africa	CI	No	4
17	Bleachers' Association	CI	Yes	2+4
18	Boots Pure Drug Company	CI	No	4
19	Bradford Dyers' Association	CI	Yes	1+2+4
20	British Cotton and Wool Dyers Association	CI	Yes	4
21	British Drug Houses	CI	Yes	4
22	British Glues and Chemicals	CI	Yes	1+4
23	British Quarrying Company	CI	Yes	1+4
24	British Rollmakers Corporation	ICS	Yes	1+4
25	Brockhouse (J.) & Co.	CI	Yes	4
26	Brooks (J. B.) & Co.	CI	No	4
27	Broom and Wade	CI	No	4
28	Brown (David) & Sons (Huddersfield)	CI	Yes	1+4
29	Budgett (H. H. and S.) and company	CI	Yes	1+4
30	Burberrys	CI	Yes	1
31	Cannock Associated Collieries	ICS	Yes	1+4
32	Cooper, McDougal & Robertson	CI	Yes	1+2+4
33	Copestake, Crampton & Company	CI	No	4
34	Cowan (Alex.) & Sons	CI	Yes	1+4
35	Crosfields Oil and Cake Company	CI	No	4
36	Crosse & Blackwell	CI	Yes	2+4
37	Denny, Mott and Dickson	CI	Yes	1+4
38	Dent, Allcroft & Co.	CI	No	4
39	Dick (W. B.) and Company	CI	No	4
40	Dixon (William) & Company, Nottingham	CI	No	4
41	Doulton & Co.	CI	Yes	1+4
42	Evans (Richd.) and Co.	ICS	No	4
43	Federated Foundries	ICS	Yes	1+4
44	Osborn (Samuel) & Co.	ICS	No	4
45	Settle Speakman & Company	ICS	No	2+4
46	Smith, Parkinson & Cole	ICS	No	4
47	South Hetton Coal Company	ICS	No	4
48	Stephenson (Robert) & Hawthorns	ICS	No	4
49	United Steel Companies	ICS	Yes	1+2+4

* ICS for Iron, Coal & Steel industry; CI for Commercial & Industrial

** the Conditions introduced in 4.4

Source: original

There are 127 companies which published both consolidated accounts and legal entity-based accounts in 1946/47 (Table 4-3). Out of these companies, 22 companies have the same

profits in the two accounts, while 105 companies show different amounts[53]. Six companies present different profits, but the directors' Section 126 statement reveals that Condition 4 is satisfied[54].

4.4.3.5 Evidence for 1950/51

In the accounting year of 1950/51, 34 British holding companies are judged to be using the equity method in the data set for this study (Table 4-3). Table 4-10 is a list of names of the companies. Since CA48 basically required publication of consolidated accounts, the main investigation was devoted to examining Condition 1. 29 companies were picked up from this examination. The other 5 companies indicate their inclusion of profits and losses of subsidiary companies in their explanation of not presenting consolidated accounts (the 8th Schedule of CA 48 requires the explanation) and Condition 5 is considered satisfied. It can be observed that only two companies satisfy Condition 2 in 1950/51. There was no new evidence which differed from other years of 1927/28, 1930/31, 1942/43 and 1946/47 except for the wordings of 8th Schedule statement.

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[53] It is true, as seen in the cases of 1942/43, that the same profits both in consolidated and legal entity-based accounts do not necessarily indicate the use of the equity method. For example, 'The above Accounts include the profit of Subsidiary Companies to the extent of the dividends recommended' (Aerated Bread Company Limited). 'The whole of the profit of H. J. Nicoll & Co. Limited (including non-recurring items) has been distributed as dividend, for which credit is taken in the above Profit and Loss Account' (Burberrys, Limited).

[54] For example, Crosse & Blackwell's Section 126 statement reveals that they employ the equity method, but that there are some exceptions. The reason of different profits shown in consolidated and legal entity-based accounts can be understood from these exceptions. In other words, subsidiary companies' undivided profits shown in the consolidated balance sheet are those of exceptional subsidiary companies (in this case Crosse & Blackwell Co., a US company and a European Produce company). As they are only exceptions, it can be said that the company was employing the equity method in general.

Table 4-10 Companies adopting the equity method 1950/51

	Company	*Industry**	*Consolidated B/S*	*Condition***
1	Aerated Bread Company	CI	Yes	1
2	Allen (Edgar) & Co.	ICS	No	5
3	Allied Brick & Tile Works	CI	Yes	1
4	Allied Ironfounders	ICS	Yes	1
5	Alvis	CI	Yes	1
6	Amalgamated Anthracite Collieries	ICS	Yes	1+2
7	Amalgamated Cotton Mills Trust	CI	Yes	1+2
8	Ambler (Jeremiah) & Sons	CI	Yes	1
9	Anglo American Asphalt Company	CI	Yes	1
10	Asprey and Company	CI	Yes	1
11	Associated Clay Industries	CI	Yes	1
12	Associated Fishers	CI	Yes	1
13	Austin (James) and Sons	CI	Yes	1
14	Avon India Rubber Company	CI	Yes	1
15	Barrow, Hepburn and Gale	CI	Yes	1
16	Bayne & Duckett	CI	Yes	1
17	Bedford (John) and Sons	ICS	No	5
18	Bertram Mills Circus	CI	No	5
19	Bradbury, Greatorex and Company	CI	No	5
20	Braime (T. F. & J. H.) (Holdings)	CI	Yes	1
21	British & American Film Press	CI	Yes	1
22	British Home Stores	CI	Yes	1
23	British Pepper & Spice Company	CI	Yes	1
24	British Photographic Industries	CI	Yes	1
25	British Syphone Company	CI	Yes	1
26	Bromilow & Edwards	CI	Yes	1
27	Broom and Wade	CI	Yes	1
28	Brooks (J. B.) & Co.	CI	Yes	1
29	Browne & Eagle	CI	Yes	1
30	Byford (D.) & Co.	CI	Yes	1
31	Darwins	ICS	Yes	1
32	Davy and United Engineering Company	ICS	Yes	1
33	Stephenson (Robert) & Hawthorns	ICS	No	5
34	Ward (Thos. W.)	ICS	Yes	1

* ICS for Iron, Coal & Steel industry; CI for Commercial & Industrial
** the Conditions introduced in 4.4
Source: original

Another finding is that the equity method is not regarded as a type of group accounting in 1950/51 any more. Accordingly, the directors of the equity method adopting companies had to note that they are not presenting group accounts unless they simultaneously prepared consolidated accounts (Table 4-11).

Table 4-11 Statements pursuant to the eighth schedule of the CA48

	Company	*Statement*
1	Allen (Edger) & Co.	(a) Group Accounts have not been prepared as the Directors are of the opinion that they would be of no real value to members of the Company in view of the relatively insignificant amounts involved. (b) The profits of the French Subsidiary Company, Acieries d'Hirson, S.A., so far as they concern members of this Company and have not been dealt with in this Company's Accounts, are as follows:- Converted at current rate of Exchange For the year to 31st December, 1950 ... ... £4,618 For the period since the French Company became a subsidiary to 31st December, 1949 ... ---- A dividend for the year ended 31st December, 1949 received from the French Subsidiary of Frs. 2,498,496 after deduction of French taxation and realising £2,537 1 8, has been credited to Profit and Loss Account in the year to 31st March, 1951. The proportion of the profits for the period prior to 31st December, 1949, attributable to the shareholding of Edgar Allen & Co. Limited amounting to £961 has been capitalised by the French Subsidiary with other reserves by increasing the nominal value of the Shares. (c) Profits and losses of the remaining three subsidiaries, since they became subsidiaries, have been credited and charged respectively in the Accounts of this Company. The aggregate amount of profits for their financial years ending with or during the last financial year of this Company amounted to £11,102 18 3
2	Bedford (John) and Sons	The Assets of the wholly owned Subsidiary Companies consist only of Balances at Bankers totalling £200, there being no liabilities; the Directors are of the opinion that the submission of Group Accounts would be of no real value to Members of the Company. No separate Profit and Loss Accounts are prepared, any Profits or Losses arising from the transactions of the Subsidiary Companies being merged in the Profit of John Bedford & Sons Ltd.
3	Bertram Mills Circus	The total grow revenue of the Subsidiary Company has been accounted for to Bertram Mills Circus Limited and is included in the Profit and Loss Account below. The Subsidiary Company has no tangible assets nor any liabilities apart from the Cash Advance of £5 shown on the Balance Sheet. In these circumstances the Directors consider the preparation of a Consolidated Balance Sheet unnecessary.
4	Bradbury, Greatorex and Company	Group accounts have not been prepared as the trading of the Subsidiary Company is incorporated in that of Bradbury, Greatorex & Co. Ltd., and its Assets and Liabilities are insignificant.
5	Stephenson (Robert) & Hawthorns	No group accounts have been prepared as they would be of no real value in view of the insignificant amounts involved in the Subsidiary Company. The trading transactions of the Subsidiary Company are undertaken by the Parent Company and are incorporated in these Accounts.

Sources: Annual Reports for the year of 1950/51.

4.5 Conclusion

This chapter has been devoted to the presentation of findings from the original empirical sources consulted to shed light on group accounting practices adopted by British companies between 1927 and 1951. There are three main findings. First, group accounting was far more common in later years than in earlier years. Second, the publication of consolidated accounts together with legal entity-based accounts (method 6) became increasingly popular, particularly after RoAP7 and CA48 took effect. Third, 13% or so of holding companies adopting group accounting employed the equity method (method 1) in the 1930s and in the 1940s, until CA48 came into force.

Given that the use of the equity method in the accounts of holding companies cannot be easily identified, unlike consolidated accounts which were usually presented under the clear titles of 'consolidated balance sheet' or 'combined balance sheet', the main part of the chapter was dedicated to presentation of evidence concerning its rate of adoption and method of adoption during the five time periods examined. It was shown that, although there are some cases where the use of the equity method could not be established with complete certainty, because of the lack of available information, it is clear that a significant number of companies consistently used that method throughout the period covered by this study.

These findings will be further analysed in the next chapter.

Chapter 5 Group Accounting Practices 1927-1950: Analysis

5.1 Introduction

The purpose of this chapter is to study further the three findings presented in the previous chapter (Chapter 4) which were as follows:

Finding1. The number and proportion of quoted companies adopting group accounting procedures grew during the period from 1927 to 1951;

Finding 2. The rate of adoption of consolidated accounts increased particularly in the periods of 1946/47 and 1950/51, which means after RoAP7 and CA48 each took effect;

Finding 3. The equity method was used by a fairly constant percentage of holding companies from 1930/31 onwards.

This chapter examines four variables relating to the companies investigated – i.e. their auditors, their size, their stock exchange (whether they were quoted on the London Official List or on a provincial stock exchange) and their type of business (Iron, Coal & Steel (ICS) or Commercial & Industrial (CI)) – to discover whether they help to explain the three findings listed above. It will be shown that the engagement of particular auditors (Cooper Brothers (CB), Thomson McLintock (TM), Price Waterhouse (PW) and Peat Marwick, Mitchell (PMM)), company size (the big companies) and where they were quoted (the Official List) seem to have some effect on the adoption of group accounting. Further, consolidated accounts are found to be adopted by almost all British holding companies in later years irrespective of who audited them, their size and where they were quoted. Moreover, it will be revealed that CB-audited companies were more likely to use the equity method in early years, but that company size and the listing arrangements appear not to have influenced use of the equity method.

5.2 Analysis

All holding companies investigated in chapter 4 are companies where information about their auditors, their issued capitals, the stock exchanges on which they were listed and their type of business are all available (see section 4.3). The availability of these data for each company makes it possible to identify (and then analyse) relationships between each variable and the group accounting practices adopted by the holding companies. The relationship between auditors and group accounting practices is first examined (sub-section 5.2.1). The relationship between issued capitals (as a proxy for size) and the group accounting methods adopted by companies is then considered (sub-section 5.2.2). The stock exchanges where companies were listed are studied in order to see if there is any regional effect on group accounting practices (sub-section 5.2.3). Finally, the relationship between type of business and group accounting practices constituent companies employ is examined (sub-section 5.2.4).

It is considered appropriate to test for these four variables in order to discover clues to help understand why the number and proportion of quoted companies adopting group accounting procedures grew during the period 1927 and 1951 (finding 1), why the rate of adoption of consolidated accounts increased particularly in the periods of 1946/47 and 1950/51 (finding 2), and why the equity method was used by a fairly constant percentage of holding companies from 1930/31 onwards (finding 3). It is recognised that the four variables are only a part of companies' many attributes, but they were examined because of the following reasons. First, the relationship between auditors and clients is important, because there is a significant literature (for example, see Edwards, 1996) indicating accountants' active role for the development of financial reporting in the U.K. Second, company size is worth examining, since most of the preceding literature selected large companies and testing for size will enable comparisons to be made between the results of

previous writings (for example, see Bircher, 1988 and Arnold and Matthews, 2002) with this study. Third, the data for a company's place of quotation was used in order to see if there are any differences in group accounting practices depending on the type of investor, based on the assumption that a provincial stock exchange will probably attract more investors who have a greater level of knowledge of local companies. Fourth, type of business (Iron, Coal and Steel or Commercial and Industrial) is focused on because the earliest British example of a consolidated statement, known so far, was published by a ICS company (Pearson & Knowles Coal and Iron Co. Ltd.) and the 'trail blazing' consolidated accounts were published by a CI company (Dunlop Rubber Co.). In other words, the two industries produced famous examples of companies publishing group accounts, and this chapter will examine whether there are any differences between these two categories in the rate of adoption of group accounting when studying a sizeable sample.

5.2.1 Auditor Analysis

This thesis first focuses on the relationship, if any, between accounting firms and the group accounting practices adopted by the holding companies that they audited. This analysis is intended to discover whether there is any connection between accounting firms and the three findings reported in chapter 4 and listed in the Introduction (section 5.1) to this chapter. In other words, is there evidence to suggest that any accounting firm:

a. encouraged the growth of group accounting (by insisting on publication of group accounts) in the period from 1927 to 1951?
b. affected the rate of adoption of consolidated accounts in 1946/47 and 1950/51?
c. favoured adoption of the equity method by clients from 1930/31 onwards?

For these purposes, those accounting firms which audited more than five companies are selected for study. It is considered that five is the minimum number of clients required in

order to make a meaningful judgement about whether the accounting firm had any preference for particular group accounting practices. When two accounting firms audit one company jointly, the client is measured as one-half for each firm.

Table 5-1 shows the accounting firms which audited more than five companies and the group accounting methods which their clients adopted.

Table 5-1 Auditor analysis

1927 28	companies employing group accounts: method 1	method 2	method 3	method 4	method 5	method 6	total	companies not employing group accounts	sample holding cos
Alfred Tongue &Co							0.0	6.5	6.5
Cooper Brothers & Co	2.5						2.5	9.0	11.5
Deloitte, Plender, Griffiths & Co						0.5	0.5	9.5	10.0
Price Waterhouse & Co			1.0			1.0	2.0	15.5	17.5
	2.5	0.0	1.0	0.0	0.0	1.5	5.0	40.5	45.5
other firms	4.5	1.0	1.0	0.0	0.0	1.5	8.0	115.5	122.5
	7.0	1.0	2.0	0.0	0.0	3.0	13.0	156.0	168.0

1930 31	companies employing group accounts: method 1	method 2	method 3	method 4	method 5	method 6	total	companies not employing group accounts	sample holding cos
Alfred Tongue &Co	1.0	0.5					1.5	6.0	7.5
Carter & Co			0.5				0.5	5.0	5.5
Cooper Brothers & Co	2.0						2.0	8.5	10.5
Deloitte, Plender, Griffiths & Co	4.0		1.0			1.0	6.0	15.0	21.0
Josolyne, Miles, Page & Co					1.0		1.0	4.5	5.5
Peat, Marwick, Mitchell & Co	2.0	1.0				1.0	4.0	19.5	22.5
Price Waterhouse & Co	2.0					3.0	5.0	21.0	25.0
Thomson McLintock & Co	1.0	0.5					1.5	4.0	5.5
	12.0	2.0	1.5	0.0	1.0	5.0	21.5	83.5	103.0
other firms	24.0	1.0	0.5	1.0	1.0	4.0	31.5	131.5	161.0
	36.0	3.0	2.0	1.0	2.0	9.0	53.0	215.0	264.0

1942 43	companies employing group accounts: method 1	method 2	method 3	method 4	method 5	method 6	total	companies not employing group accounts	sample holding cos
Alfred Tongue &Co						1.0	1.0	6.0	7.0
Cooper Brothers & Co	3.0					1.0	4.0	7.0	10.0
Deloitte, Plender, Griffiths & Co	3.0	2.0	1.0			1.5	7.5	17.0	23.5
Peat, Marwick, Mitchell & Co	7.5	3.0				7.0	17.5	17.0	31.0
Price Waterhouse & Co	4.0					2.0	6.0	24.0	29.0
Sharp, Parsons & Co							0.0	5.0	5.0
Thomson McLintock & Co	2.5					3.0	5.5	7.0	10.5
	20.0	5.0	1.0	0.0	0.0	15.5	41.5	83.0	116.0
other firms	21.0	4.0		1.0	1.0	25.5	52.5	159.0	207.0
	41.0	9.0	1.0	1.0	1.0	41.0	94.0	242.0	323.0

1946 47	companies employing group accounts: method 1	method 2	method 3	method 4	method 5	method 6	total	companies not employing group accounts	sample holding cos
Alfred Tongue &Co						1.0	1.0	6.0	7.0
Carter & Co	1.0			1.0		3.0	5.0	3.0	7.0
Cooper Brothers & Co	3.0					6.0	9.0	3.0	9.0
Deloitte, Plender, Griffiths & Co	3.0					9.0	12.0	13.0	24.0
Gane, Jackson, Jefferys & Freeman	1.0	1.0				1.0	3.0	2.0	5.0
Josolyne, Miles, Page & Co	1.0				1.0	3.0	5.0	1.0	6.0
Kerr, Macleod & Macfarian						1.0	1.0	4.0	5.0
Moores, Carson & Watson	1.0						1.0	5.0	6.0
Peat, Marwick, Mitchell & Co	4.0	1.0				14.0	19.0	15.0	32.0
Price Waterhouse & Co	9.0	1.0				16.5	26.5	10.5	30.0
Sharp, Parsons & Co	2.0		1.0			1.0	4.0	2.0	5.0
Thomson McLintock & Co	2.0					8.0	10.0	4.0	12.0
Turquand, Youngs, McAulifee & Co		1.0					1.0	6.0	7.0
	27.0	4.0	1.0	1.0	1.0	63.5	97.5	74.5	155.0
other firms	22.0	4.0	2.0		1.0	63.5	92.5	129.5	209.0
	49.0	8.0	3.0	1.0	2.0	127.0	190.0	204.0	364.0

1950 51	companies employing group accounts: method 1	method 2	method 3	method 4	method 5	method 6	other*	total	companies not employing group accounts	sample holding cos
Binder, Hamlyn & Co						5.5		5.5		5.5
Cooper Brothers & Co	2.0					14.0		16.0		15.0
Deloitte, Plender, Griffiths & Co		1.0				16.5		17.5		17.5
Franklin, Wild & Co						3.0		3.0	2.0	5.0
Moores, Carson & Watson		1.0				4.0		5.0	1.0	6.0
Peat, Marwick, Mitchell & Co	7.0	2.0				26.0		35.0		32.5
Price Waterhouse & Co	3.5	1.0				32.0		36.5		35.5
Sharp, Parsons & Co	1.0					6.0		7.0		6.0
Thomson McLintock & Co	2.0					12.0		14.0		12.0
Whinney, Smith & Whinney						7.0	1.0	8.0		8.0
	15.5	5.0	0.0	0.0	0.0	126.0	1.0	147.5	3.0	143.0
other firms	18.5	11.0	1.0		2.0	245.0	3.0	280.5	26.0	283.0
	34.0	16.0	1.0	0.0	2.0	371.0	4.0	428.0	29.0	426.0

*other methods are explained in Table 4-3 of chapter 4

Source: original

The first question ('is there evidence to suggest that any accounting firm encouraged the growth of group accounting?') can be answered by consulting the 'total' column and 'sample holding companies' column in Table 5-1. In 1927/28, 21.7% (=2.5/11.5) clients of Cooper Brothers & Co. (CB) and 11.4% (=2/17.5) clients of Price Waterhouse & Co. (PW) adopted group accounting. These proportions are higher than overall average (7.7% = 13/168). This finding suggests that these two accounting firms were a little more willing than other firms to encourage or allow their clients to publish group accounts in 1927/28. A similar pattern of certain accounting firms having a greater proportion of clients adopting group accounting procedures also applies in the other years studied and this phenomenon is further examined in Table 5-2.

In Table 5-2, CB has more clients than average who adopted group accounting in 1927/28, 1942/43, 1947/48 and 1950/51. Thomson McLintock & Co. (TM) is also on the list in four years (1930/31, 1942/43, 1947/48 and 1950/51). PW is on the list in three years (1927/28, 1947/48 and 1950/51) and Peat, Marwick, Mitchell & Co. (PMM) again in three years (1942/43, 1946/47 and 1950/51). Other accounting firms appear on the list less than twice for the studied five years. It is therefore possible to suggest that the four accounting firms and their clients may have influenced the rate of adoption in the period from 1927 to 1951.

Table 5-2 Accounting firms whose clients reveal above average rates of adoption of group accounting

accounting firm	*total clients (a)*	*clients adopting group accounting (b)*	*(b)/(a)*	*average*
1927/28				
1 Cooper Brothers & Co.	11.5	2.5	21.7%	7.7%
2 Price, Waterhouse & Co.	17.5	2.0	11.4%	7.7%

1930/31				
1 Deloitte, Plender, Griffiths & Co.	21.0	6.0	28.6%	20.1%
2 Thomson McLintock & Co.	5.5	1.5	27.3%	20.1%
1942/43				
1 Peat, Marwick, Mitchell & Co.	31.0	17.5	56.5%	29.1%
2 Thomson McLintock & Co.	10.5	5.5	52.4%	29.1%
3 Cooper Brothers & Co.	10.0	4.0	40.0%	29.1%
4 Deloitte, Plender, Griffiths & Co.	23.5	7.5	31.9%	29.1%
1947/48				
1 Cooper Brothers & Co.	9.0	9.0	100.0%	52.2%
2 Price, Waterhouse & Co.	30.0	26.5	88.3%	52.2%
3 Josolyne, Miles, Page & Co.	6.0	5.0	83.3%	52.2%
4 Thomson McLintock & Co.	12.0	10.0	83.3%	52.2%
5 Sharp, Parsons & Co.	5.0	4.0	80.0%	52.2%
6 Carter & Co.	7.0	5.0	71.4%	52.2%
7 Gane, Jackson, Jefferys & Freeman	5.0	3.0	60.0%	52.2%
8 Peat, Marwick, Mitchell & Co.	32.0	19.0	59.4%	52.2%
1950/51				
1 Sharp, Parsons & Co.	6.0	7.0	116.7%	100.5%
2 Thomson McLintock & Co.	12.0	14.0	116.7%	100.5%
3 Peat, Marwick, Mitchell & Co.	32.5	35.0	107.7%	100.5%
4 Cooper Brothers & Co.	15.0	16.0	106.7%	100.5%
5 Price, Waterhouse & Co.	35.5	36.5	102.8%	100.5%

note: companies adopting plural methods are counted multiple times, which results in the percentages in excess of 100 in the table (see Table 4-3 in Chapter 4).

Source: original

The second question ('is there evidence to suggest that any accounting firm affected the rate of adoption of consolidated accounts in the later years?') can be answered by consulting proportions of clients adopting consolidated accounts (method 6) compared with clients adopting any method of group accounting. It is assumed for the purpose of this study that, where more than one half (50%) of clients which adopt any method of group accounting are adopting consolidated accounts, the accounting firm and its clients favour the publication of consolidated accounts. For the second question to be answered positively, one would expect to find that DPG was the type of firm that would prove responsible for the increased rate of adoption of consolidated accounts in later years.

Table 5-3 lists the auditing firms where more than 50% of group-accounts-adopting clients publish consolidated accounts in the period from 1927 to 1951. In Table 5-3, it is clear that there is a big difference between the three earlier years (1927/28, 1930/31, 1942/43)

and the two later years (1946/47 and 1950/51). To put it more specifically, in the earlier years one or two accounting firms appear to favour the publication of consolidated accounts, whereas in the later years most of the clients of the accounting firms investigated adopted that method. This finding suggests that the reason for the increasing rate of adoption of consolidated accounts in later years is not attributable to any specific firm(s) but it was an overall tendency among the accounting firms to accept consolidated accounts more than in earlier years. In other words, the second question produces a negative answer.

Table 5-3 Accounting firms where more than 50% of group-accounts-adopting clients publish consolidated accounts

	Accounting firm	*clients adopting group acc. (a)*	*clients adopting method 6 (b)*	*(b)/(a)*
1927/28				
1	Deloitte, Plender, Griffiths & Co.	0.5	0.5	100.0%
1930/31				
1	Price, Waterhouse & Co.	5.0	3.0	60.0%
1942/43				
1	Alfred Tongue & Co.	1.0	1.0	100.0%
2	Thomson McLintock & Co.	5.5	3.0	54.5%
1946/47				
1	Alfred Tongue & Co.	1.0	1.0	100.0%
2	Kerr, Macleod & Macfarian	1.0	1.0	100.0%
3	Thomson McLintock & Co.	10.0	8.0	80.0%
4	Deloitte, Plender, Griffiths & Co.	12.0	9.0	75.0%
5	Peat, Marwick, Mitchell & Co.	19.0	14.0	73.7%
6	Cooper Brothers & Co.	9.0	6.0	66.7%
7	Price, Waterhouse & Co.	26.5	16.5	62.3%
8	Josolyne, Miles, Page & Co.	5.0	3.0	60.0%
9	Carter & Co.	5.0	3.0	60.0%
1950/51				
1	Binder, Hamlyn & Co.	5.5	5.5	100.0%
2	Franklin, Wild & Co.	3.0	3.0	100.0%
3	Deloitte, Plender, Griffiths & Co.	17.5	16.5	94.3%
4	Price, Waterhouse & Co.	36.5	32.0	87.7%
5	Cooper Brothers & Co.	16.0	14.0	87.5%
6	Whinney, Smith & Whinney	8.0	7.0	87.5%
7	Sharp, Parsons & Co.	7.0	6.0	85.7%

8	Thomson McLintock & Co.	14.0	12.0	85.7%
9	Moores, Carson & Watson	5.0	4.0	80.0%
10	Peat, Marwick, Mitchell & Co.	35.0	26.0	74.3%

Source: original

The third question ('is there evidence to suggest that any accounting firm favoured adoption of the equity method from 1930/31 onwards?') can be answered by consulting proportions of clients adopting the equity method (method 1) compared with clients adopting any other method of group accounting. It is assumed for the purpose of this study that, if more than one half (50%) of clients which adopt any method of group accounting adopted the equity method, the accounting firm is favourably inclined towards the use of that method. For example, 100% (=2.5/2.5) of the clients of CB who were holding companies adopted the equity method in 1927/28 (Table 5-1). It is assumed, therefore, that CB is favourably inclined towards the adoption of that method.

Table 5-4 lists the auditing firms where more than 50% of the clients who were holding companies adopted the equity method in the period from 1927 to 1951. As it can be seen, no accounting firm had the majority of its clients adopting the equity method in 1946/47 or in 1950/51. This fact suggests that there was no accounting firm which showed a consistent preference for the equity method during this period.

Another finding from Table 5-4 is that CB appears on the list in three years (1927/28, 1930/31 and 1942/43), although the proportion of clients adopting that method declined. It can be seen that 100% of clients in 1927/28 and 1930/31 and 75% in 1942/43 are users of the equity method. This proportion is far higher than for any other firm.

Table 5-4 Accounting firms where more than 50% of group-accounts-adopting clients use the equity method

Accounting firm	*Clients adopting group acc. (a)*	*clients adopting method I (b)*	*(b)/(a)*
1927/28			
1 Cooper Brothers & Co.	2.5	2.5	100.0%
1930/31			
1 Cooper Brothers & Co.	2.0	2.0	100.0%
2 Deloitte, Plender, Griffiths & Co.	6.0	4.0	66.7%
3 Alfred Tongue & Co.	1.5	1.0	66.7%
4 Thomson McLintock & Co.	1.5	1.0	66.7%
1942/43			
1 Cooper Brothers & Co.	4.0	3.0	75.0%
2 Price, Waterhouse & Co.	6.0	4.0	66.7%
1946/47			
None			
1950/51			
None			

Source: original

5.2.2 Size Analysis

The second stage of the analysis is intended to find out if there is any connection between company size and the three findings reported in chapter 4. In other words, is there evidence to suggest that size of the holding company:

a. encouraged the rate of adoption of group accounting in the period from 1927 to 1951?

b. affected the increasing rate of adoption of consolidated accounts in 1946/47 and 1950/51?

c. favoured the adoption of the equity method by clients from 1930/31 onwards?

The companies investigated are divided into four categories, according to their amount of issued capital. Table 5-5 summarises for each quartile (quartile 1 contains the 25% largest companies) and group accounting method adopted by the constituent companies.

Table 5-5 Size analysis

1927 28	*companies employing group accounts*							*companies not employing group accounts*	*sample holding cos*
	method 1	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*		
1st quartile	3	1	2			2	8	35	42
2nd quartile	3						3	39	42
3rd quartile						1	1	41	42
4th quartile	1						1	41	42
	7	1	2	0	0	3	13	156	168

1930 31	*companies employing group accounts*							*companies not employing group accounts*	*sample holding cos*
	method 1	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*		
1st quartile	8	1	2			4	15	52	66
2nd quartile	11	1		1		2	15	53	66
3rd quartile	6	1			1	2	10	57	66
4th quartile	11				1	1	13	53	66
	36	3	2	1	2	9	53	215	264

1942 43	*companies employing group accounts*							*companies not employing group accounts*	*sample holding cos*
	method 1	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*		
1st quartile	9	4	1	1		18	33	53	81
2nd quartile	13	4				12	29	59	81
3rd quartile	9	1				7	17	66	82
4th quartile	10				1	4	15	64	79
	41	9	1	1	1	41	94	242	323

1946 47	*companies employing group accounts*							*companies not employing group accounts*	*sample holding cos*
	method 1	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*		
1st quartile	13	1	2			48	64	40	91
2nd quartile	15	5		1	1	39	61	42	92
3rd quartile	11	1				20	32	61	89
4th quartile	10	1	1		1	20	33	61	92
	49	8	3	1	2	127	190	204	364

1950 51	*companies employing group accounts*								*companies not employing group accounts*	*sample holding cos*
	method 1	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*other**	*total*		
1st quartile	8	3	1			99	1	112	5	107
2nd quartile	10	5				94	1	110	7	109
3rd quartile	10	4			1	88	1	104	8	103
4th quartile	6	4			1	90	1	102	9	107
	34	16	1	0	2	371	4	428	29	426

*other methods are explained in Table 4-3 of chapter 4

Source: original

The first question (concerning the relationship between size and the adoption of any form of group accounts) can be answered by consulting the 'total' column and 'sample holding companies' column in Table 5-5. It is possible to conclude that larger companies were more likely to publish group accounts until this became a regulatory requirement for all companies.

For example, in 1927/28, eight (19.0%) out of the 42 largest companies prepared group accounts compared with just one (2.4%) of the 42 smallest companies and 13 (7.7%) of companies in the full sample. In 1946/47, 125 (68.3%) companies in the top two quartiles published group accounts compared with 65 (35.9%) in the lower two quartiles.

The second question (concerning the relationship between size and the publication of consolidated accounts) can be answered by studying the 'method 6' column of Table 5-5 compared to the total column. It is possible to conclude that in the three earlier years (1927/28, 1930/31 and 1942/43) the largest quartile were most likely, and the smallest quartile of companies were least likely, to publish consolidated accounts, whereas in later years (1947/48 and 1950/51) there was no substantial difference between big and small companies. For example, in 1930/31, four (26.7%) out of the 15 largest companies, two (13.3%) of 15 second largest companies and two (20.0%) of the 10 second smallest companies published consolidated accounts compared with just one (7.7%) of the 13 smallest companies adopting any form of group accounting. A similar contrast can be seen in 1942/43 when 54.5% (=18/33) of the largest companies, 41.4% (=12/29) of the second largest companies and 41.2% (=7/17) of the second smallest companies prepared consolidated accounts whereas only 26.7% (=4/15) of the smallest companies presented their accounts in this manner. On the other hand, in 1946/47, 60.6% (=20/33) of the smallest companies adopted consolidated accounts and the proportion is not substantially different from 75.0% (=48/64) of the largest companies, 63.9% (=39/61) of the second largest companies and 62.5% (=20/32) of the second smallest companies. In 1950/51, 88.4% (=99/112), 85.5% (=94/110), 84.6% (=88/104) and 88.2% (=90/102) of companies in the 1st, 2nd, 3rd and 4th quartile respectively published consolidated accounts.

The third question (concerning the relationship between size and the use of the equity method) can be answered by consulting the contents of the 'method 1' column and the total

column of Table 5-5. It seems reasonable to say that the use of the equity method has nothing to do with the company size. For example, in 1930/31, 19 (63.3%) out of the 30 companies in the top two quartiles adopted the equity method, while 17 (73.9%) out of the 23 companies in the lower two quartiles did the same. In 1950/51, 18 (8.1%) of companies in the top two and 16 (7.8%) of the lower two adopted the equity method.

5.2.3 Stock Exchange-based Analysis

The third stage of the analysis presented in this chapter considers whether the three findings reported in chapter 4 and listed in the Introduction of this chapter can be explained in terms of where companies were listed. In other words, is there evidence to demonstrate a difference between companies listed in the Official List and in the Provinces in terms of:

a. the growth of group accounting in the period from 1927 to 1951?

b. the increasing rate of adoption of consolidated accounts in 1946/47 and 1950/51?

c. the preference for the equity method from 1930/31 onwards?

For the purpose of this analysis, those companies listed on both the Official List and provincial stock exchanges are allocated to the former. Table 5-6 presents the findings.

Table 5-6 Stock exchange-based analysis

	companies employing group accounts							companies not employing group accounts	sample holding cos
1927 28	*method 1*	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*	*accounts*	*cos*
official list	7	1	2			3	13	107	119
provinces							0	49	49
total	7	1	2	0	0	3	13	156	168

	companies employing group accounts							companies not employing group accounts	sample holding cos
1930 31	*method 1*	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*	*accounts*	*cos*
official list	27	2	2	1	1	7	40	136	172
provinces	9	1			1	2	13	79	92
total	36	3	2	1	2	9	53	215	264

	companies employing group accounts							companies not employing group accounts	sample holding cos
1942 43	*method 1*	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*	*accounts*	*cos*
official list	30	8	1	1		32	72	157	218
provinces	11	1			1	9	22	85	105
total	41	9	1	1	1	41	94	242	323

	companies employing group accounts							companies not employing group accounts	sample holding cos
1946 47	*method 1*	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	*total*	*accounts*	*cos*
official list	33	7	3	1	1	98	143	118	237
provinces	16	1			1	29	47	86	127
total	49	8	3	1	2	127	190	204	364

	companies employing group accounts								companies not employing group accounts	sample holding cos
1950 51	*method 1*	*method 2*	*method 3*	*method 4*	*method 5*	*method 6*	other*	*total*	*group accounts*	*cos*
official list	30	12	1		2	323	4	372	18	361
provinces	4	4				48		56	11	65
total	34	16	1	0	2	371	4	428	29	426

*other methods are explained in Table 4-3 of chapter 4

Source: original

The first question (concerning a possible relationship between place of quotation and the adoption of some form of group accounts) can be answered by consulting the 'total' column and 'sample holding companies' column in Table 5-6. It can be seen that companies in the Official List were more likely to adopt group accounts throughout the period studied. For example, in 1927/28 10.9% (=13/119) Official List companies published group accounts, whereas no Provincial companies did so. Consistent with this finding, 23.3% (=40/172) in 1930/31, 33.0% (=72/218) in 1942/43, 60.3% (=143/237) in 1946/47 and 103.3% (=372/361)

in 1950/51 are all substantially higher proportions than for Provincially-listed companies (14.1%, 21.0%, 37.0% and 86.2% respectively).

The second question (concerning a possible relationship between place of quotation and the publication of consolidated accounts) can be answered by relating the contents of the 'method 6' column to the 'total' group accounting column of Table 5-6. It seems that there is little difference between companies in Official List and in Provinces in terms of the rate of adoption of consolidated accounting practices throughout the period. For example, in 1930/31, 7 (17.5%) out of 40 Official List companies and 2 (15.4%) out of 13 Provincial companies adopted consolidated accounts. Similarly, 44.4% (=32/72), 68.5% (=98/143) and 86.8% (=323/372) of Official companies published consolidated accounts in 1942/43, 1946/47, and 1950/51 respectively and the proportions is not markedly different from those of Provincial companies which were 40.9% (=9/22), 61.7% (=29/47) and 85.7% (=48/56) for the same periods.

The third question (concerning a possible relationship between place of quotation and the adoption of equity accounting) can be answered by relating the 'method 1' column to the 'total' group accounting column of Table 5-6. It seems reasonable to say that the equity method is slightly more favoured by Provincial companies, but the difference is not marked. For example, in 1930/31, 27 (67.5%) out of 40 Official List companies adopted the equity method while 9 (69.2%) out of 13 Provincial companies did the same. Similarly, 41.7% (=30/72), 23.1% (=33/143) and 8.1% (=30/372) of Official List companies employed the equity method in 1942/43, 1946/47 and 1950/51 respectively and the proportions of Provincial companies adopting the same method in the same accounting periods are 50.0% (=11/22), 34.0% (=16/47) and 7.1% (=4/56) respectively.

5.2.4 Industry Analysis

The last stage of the analysis presented in this chapter considers whether further light can be shed on the three findings reported in chapter 4 by comparing the group accounting practices of the two different types of business covered in this study. In other words, is there evidence to suggest that the type of business undertaken by the holding company:

a. encouraged the rate of adoption of group accounting in the period from 1927 to 1951?
b. affected the increasing rate of adoption of consolidated accounts in 1946/47 and 1950/51?
c. favoured the adoption of the equity method by clients from 1930/31 onwards?

The companies investigated are divided into two groups according to their type of business, distinguishing between iron, coal and steel (ICS) companies on the one hand and commercial and industrial (CI) companies on the other. Table 5-7 presents the findings.

Table 5-7 Industry analysis

1927 28	companies employing group accounts							companies not employing group accounts	sample holding cos
	method 1	method 2	method 3	method 4	method 5	method 6	total		
ICS	2					1	3	78	81
CI	5	1	2			2	10	78	87
total	7	1	2	0	0	3	13	156	168

1930 31	companies employing group accounts							companies not employing group accounts	sample holding cos
	method 1	method 2	method 3	method 4	method 5	method 6	total		
ICS	6	1			1	3	11	86	96
CI	30	2	2	1	1	6	42	129	168
total	36	3	2	1	2	9	53	215	264

1942 43	companies employing group accounts							companies not employing group accounts	sample holding cos
	method 1	method 2	method 3	method 4	method 5	method 6	total		
ICS	11	5				17	33	72	100
CI	30	4	1	1	1	24	61	170	223
total	41	9	1	1	1	41	94	242	323

1946 47	companies employing group accounts							companies not employing group accounts	sample holding cos
	method 1	method 2	method 3	method 4	method 5	method 6	total		
ICS	12	3				36	51	65	111
CI	37	5	3	1	2	91	139	139	253
total	49	8	3	1	2	127	190	204	364

1950 51	companies employing group accounts								companies not employing group accounts	sample holding cos
	method 1	method 2	method 3	method 4	method 5	method 6	other**	total		
ICS	8	5				72	2	87	6	91
CI	26	11	1		2	299	2	341	23	335
total	34	16	1	0	2	371	4	428	29	426

*ICS for Iron, Coal & Steel industry; CI for Commercial & Industrial
**other methods are explained in Table 4-3 of chapter 4

Source: original

The first question (concerning a possible relationship between type of business and the adoption of some form of group accounts) can be answered by consulting the 'total' column and 'sample holding companies' column in Table 5-7. It can be seen that CI companies are more likely to adopt group accounts in 1927/28 and 1930/31, but there seems no big difference between ICS companies and CI companies after 1942/43. For example, in 1927/28, 10 (11.5%) out of 87 CI companies prepared group accounts compared with 3

(3.7%) of the 81 ICS companies. In 1930/31, 42 (25.0%) out of 168 CI companies published group accounts compared with 11 (11.5%) of 96 ICS companies. After 1942/43, the proportion of ICS companies and CI companies adopting group accounts show insubstantial differences, since 33.0% (=33/100), 46.0% (=51/111) and 95.6% (=87/91) of ICS companies presented group accounts in 1942/43, in 1946/47 and 1950/51 respectively, whereas 27.3% (=61/223), 54.9% (=139/253) and 101.8% (=341/335) of CI companies published group accounts in the same accounting years.

The second question (concerning the relationship between type of business and the adoption of consolidated accounts) can be answered by studying the 'method 6' column and the total column of Table 5-7. It seems possible to say that the ICS companies are slightly more likely to prepare consolidated accounts than CI companies. For example, in 1930/31, 3 (27.3%) out of 11 ICS companies adopted consolidated accounts, while 6 (14.3%) out of 42 CI companies did the same. Similarly, 51.5% (=17/33) and 70.6% (=36/51) of ICS companies presented consolidated accounts in 1942/43 and 1947/48 compared to 39.3% (=24/61) and 65.5% (=91/139) of CI companies. In 1950/51, the position reverses with 82.8% (=72/87) of ICS companies and 87.7% (=299/341) CI companies publishing consolidated accounts.

The third question (concerning the relationship between type of business and the use of the equity method) can be answered by consulting the contents of the 'method 1' column and the total column of Table 5-7. It can be seen that CI companies show a higher rate of adoption of the equity method compared with ICS companies up until 1946/47. For example, in 1930/31, 30 (71.4%) out of 42 CI companies employed the equity method compared to 6 (54.5%) of the 11 ICS companies. Similarly, 49.2% (=30/61) and 26.6% (=37/139) of CI companies adopted the equity method in 1942/43 and 1946/47 respectively, whereas 33.3% (=11/33) and 23.5% (=12/51) of ICS companies used the equity method in the same

accounting years. In 1950/51, the position turned around and more ICS companies (9.2%) employed the equity method than CI companies (7.6%). Therefore it is observed that the CI companies are slightly more likely to employ the equity method than ICA companies until 1946/47.

5.2.5 Summary

Above, four variables have been examined – company auditor, company size, stock exchange on which the company was quoted, and type of business – to try to augment the findings presented in chapter 4. The result of this exercise is now summarised in Table 5-8 below.

Table 5-8 Summary of the results from four analyses

	Group accounts (methods 1-6)	*Consolidated accounts (method 6)*	*Equity method (method 1)*
Auditors	Companies audited by any of CB, TM, PW, PMM were more likely to publish group accounts throughout the period.	In the three earlier years (1927/28, 1930/31, 1942/43) there was no relation with any specific accounting firm, and in the later years (1946/47, 1950/51) companies audited by most of the accounting firms adopted consolidated accounts	In the three earlier years (1927/28, 1930/31, 1942/43) companies audited by CB were more likely to adopt the equity method, whereas in the later years (1946/47, 1950/51) companies audited by accounting firms investigated were unlikely to adopt the equity method
Size	Before CA48 (1927/28, 1930/31, 1942/43, 1946/47) larger companies were more likely to publish group accounts, while after CA48 (1950/51) there was no substantial difference between big and small companies.	In the three early years (1927/28, 1930/31, 1942/43) the smallest quartile of companies were unlikely to publish consolidated accounts, whereas in later years (1946/47, 1950/51) there was no substantial difference between big and small companies	There was little relationship throughout the period.
Stock exchange	Companies on Official List were more likely to adopt group accounts throughout the period.	There was little relationship throughout the period.	There was little relationship throughout the period.
Type of business	In the two early years (1927/28, 1930/31) CI companies are more likely to adopt group accounts, while there was no big difference in 1942/43, 1946/47 and 1950/51.	The ICS companies are slightly more likely to prepare consolidated accounts than CI companies until 1946/47.	The CI companies are slightly more likely to employ the equity method than ICS companies until 1946/47.

*CB for Cooper Brothers & Co.; TM for Thomson McLintock & Co.; PW for Price Waterhouse & Co.; PMM for Peat, Marwick, Mitchell & Co.
**ICS for Iron, Coal & Steel industry; CI for Commercial and Industrial

5.3 Consistency with previous literature

5.3.1 Big companies, auditing firms and group accounting

It was revealed that the engagement of particular auditors (CB, TM, PW and PMM) and company size (the big companies) seem to have some effect on the adoption of group accounting practices by companies. The finding is consistent with previous literature in two points.

First, most of the preceding literature selected large companies[55] (Loudon, 1931; Bircher, 1988; Arnold and Matthews, 2002) in examining the adoption rate of consolidated accounts by British holding companies. Bircher (1988: 5) explained the selection that 'a sample of large companies was ... more likely to include those companies that establish best practice' (Bircher, 1988: 5). When the 'best practice' is represented by any form of group accounting, this study confirms that big companies employed best practice. It is unknown from the evidence used in this study why larger companies were more likely to use group accounts. One possible reason is that there may have been a greater divorce between management and shareholders and more pressure from shareholders in such companies for more information. This point will be raised again in chapter 9 as a further possible research theme.

Second, the role of the accountancy profession in the adoption of group reporting practices by companies was observed in this study as well as in the previous literature. It has been revealed (chapter 2) that accountants such as Garnsey and de Paula exerted an important influence on the development of group accounting in the UK (see for example, Kitchen, 1972 and Edwards, 1996). The finding in this study indicates that also the larger auditing firms

[55] Loudon selected 103 large public companies (excluding insurance companies, banks, investment trust companies etc.) at random whose shares were quoted on the Stock Exchange (Loudon, 1931: 679). Bircher investigated the 40 largest holding companies, by market capitalisation, taken from the commercial section of the Stock Exchange Year Book (Bircher, 1988: 5). Arnold and Matthews also dealt with 50 largest companies from Chandler's list of the 200 largest industrial enterprises by market value for 1919, 1930 and 1948 and Wardley's 50 largest companies by market value, using somewhat different criteria, for 1904-5 and 1934-5 (Arnold and Matthews, 2002: 7).

have contributed to the introduction of group accounting by British holding companies. Edwards (1996: 53) introduced a term of 'professional initiatives in UK' when describing 'the period when leadership in the development of financial reporting practices was firmly in the hands of the accountancy profession'. The finding of this study is also consistent with this description.

It is also important to note that several methods of group accounting continued to be employed by British holding companies throughout the period from 1927 to 1951, although publishing subsidiary companies' balance sheets (method 2), publishing combined accounts of subsidiary companies (method 3), publishing combined accounts of the group without consolidation procedures (method 4) and publishing consolidated accounts without the holding company's individual accounts (method 5) were relatively less popular methods throughout the entire study period. Methods that can be said to be the most common ways of presenting group information during the period investigated are consolidated accounts published in addition to the holding company's statutory accounts (method 6) and the inclusion of profits and losses of subsidiary companies in the holding company's statutory (legal entity-based) accounts irrespective of dividends actually declared or paid (method 1)[56]. To put it chronologically, the development of group accounting can be interpreted as follows, according to the Table 4-3 in Chapter 4. In the 1920s and 1930s, the equity method (method 1) was the most used form of group accounting by British holding companies, while after 1942/43 the number of companies adopting consolidated accounts (method 6) exceeded the number of those using the equity method, and consolidation became almost the universal method after the CA48 took effect, with the equity method by then far less used[57]. The

[56] For example, in the accounting year of 1942/43, 12.7% of sampled British holding companies adopted the equity method and the same percentage (12.7%) of companies published consolidated accounts (see Table 4-3 in Chapter 4). The overall percentage of companies adopting any form of group accounting was 29.1%, which means most of them employed either the equity method or consolidated accounts.

[57] The proportion of companies adopting consolidated accounts in 1946/47 was 34.9% and it became 87.1% in 1950/51 (Table 4-3 in Chapter 4). On the contrary, the equity method was used by 13.5%

development of group accounting as a whole reflects the dynamics surrounding the employment of these two methods.

5.3.2 Consolidated accounts and the impact of regulations

It was also revealed in section 5.2 that the adoption of consolidated accounts bears little relationship with any of the four variables studied. Rather, what was clear is that most companies adopted consolidated accounts after professional guidance and statutory regulations were issued. In 1946/47, which was an accounting period that occurred after the business community was made aware of the profession's judgment about what constituted best practice through the publication of RoAP7, companies adopting consolidation increased to 34.9% from 12.7% in 1942/43. After CA48 took effect, the proportion reached 87.1% in 1950/51 (Table 4-3 in Chapter 4). The finding is consistent with previous literature in that regulations (RoAP7 and CA48) are considered to have played a significant impact on group accounting practices (Bircher, 1988; Arnold and Matthews, 2002). Table 5-9 shows the comparative figures for the three studies concerning proportions of companies adopting consolidated accounts. It seems possible to draw attention to the existence of more robust evidence in support of finding 2 provided by this study, given the far larger sample of companies compared with those examined by Bircher (1988) and by Arnold and Matthews (2002).

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companies in 1946/47 and 8.0% in 1950/51.

Table 5-9 Proportion of companies adopting consolidated accounts

	1920	1927/28	1930/31	1933	1935	1938/39	1942/43	1944/45	1946/47	1947/48	1950	1950/51	sample number
Bircher 1988						22.5%		32.5%		74.0%			40
Arnold & Matthews 2002	0.0%				14.0%						100%		50
this study		1.8%	3.4%				12.7%		34.9%			87.1%	309 (ave)

Source: Arnold & Matthews, 2002; Bircher, 1988.

However, it must be added here that the number and proportion of companies publishing consolidated accounts did increase even *before* the regulations took effect. In 1927/28, there were only 1.8% of sampled holding companies publishing consolidated accounts, but the proportion rose to 3.4% in 1930/31 and 12.7% in 1942/43 (Table 4-3 in Chapter 4). The rise from 1930/31 to 1942/43 seems worthy of attention, because the revelations in the Royal Mail case (1931) and the publication of Dunlop Rubber's 'trail blazing' consolidated accounts (1933) occurred between these years. The growth in use of consolidated accounts provides further empirical support for the notion of these events to having been influential, as previous literature has suggested (see, for example, Edwards, 1989a). Yet, it is clearly the case that these two events did not result in consolidated accounts becoming widely adopted by British holding companies, since only 12.7% of the studied companies prepared consolidated accounts as late as 1942/43 according to the present study. As this study and that of Bircher (1988) reveal, the effect of these events on larger companies may have been greater.

5.3.3 The equity method supported by accountants

The finding that the equity method was the most used group accounting practice in 1920s and 1930s is consistent with previous literature. Edwards and Webb (1984) revealed that various methods of group accounting were used by British holding companies and that the equity

method was fairly popular, especially in early years until 1933, when Dunlop Rubber published the famous accounts.

It was also revealed that in the three earlier years (1927/28, 1930/31 and 1942/43) companies audited by Cooper Brothers & Co. (CB) were more likely to adopt the equity method. None of the other variables (company size, stock exchange and type of business) appear to possess any explanatory potential for the use of the equity method. The finding concerning a relationship between company auditor and use of the equity method is consistent with the fact that D'Arcy Cooper, former senior partner in CB, strongly supported adoption of the equity method (see, for example, D'Arcy Cooper, 1925a, b, c). This point will be examined further in Chapter 6.

5.4 Conclusion

In this chapter, four variables relating to companies (their auditors, their size, their stock exchange, and their type of business) were used to analyse the three findings presented in Chapter 4. As a result, the three findings can be elaborated upon as follows.

Finding 1. The growth in number and proportion of companies adopting group accounting practices seems to have born some relationship to the engagement of particular auditors (Cooper Brothers & Co., Thomson McLintock & Co., Price Waterhouse & Co. and Peat, Marwick, Mitchell & Co.), to company size (the big companies) and to the stock exchange (Official List).

Finding 2. The sharp upturn in the rate of adoption of consolidated accounts in the periods 1946/47 and 1950/51, which means after RoAP7 and CA48 each took effect, seems to have no strong relationship with any of the four variables.

Finding 3. The equity method was used by a fairly constant percentage of holding

companies from 1930/31 onwards, and in the early years the influence of Cooper Brothers & Co. seems to have been noteworthy.

In most respects, the above findings are consistent with the previous literature. Most important for the purpose of this study, which employs the theory of path dependence to provide a fundamental answer to the research question, is Finding 1, which reveals an overall tendency of British holding companies' adoption rate of group accounts. This shows that the most common practice between 1927 and 1943 among the holding companies studied, was to publish only legal entity-based accounts. Table 4-3 in chapter 4 shows that 92.9% of holding companies in this study in 1927/28, 81.4% of companies in 1930/31, and 74.9% of companies in 1942/43 did not adopt any form of group accounting. At these dates, therefore, only a relatively small proportion of holding companies adopted equity accounting or published consolidated accounts. Further, given the known tendency of larger holding companies, those audited by such firms as CB, TM, PW and PMM, and those listed on the Official List to be more likely to publish group accounts, the overwhelming proportion of other holding companies published no group accounts until the late 1940s. Applying the theory of path dependence, it can be concluded that the practice of publishing no group accounts was shared by a large number of holding company directors and institutionalised and thus became slow to change.

But why was the practice of publishing only legal entity based accounts the most popular action among holding company directors in 1927/28, 1930/31 and 1942/43? The explanation put forward in this thesis is that it provides evidence of path dependent behaviour on the part of the directors of British holding companies. Even where they adopted some form of group accounting, it was equity accounting which remained by far the most popular method in 1927/28 and 1930/31 (Finding 3). Even in 1942/43, there were still as many holding companies adopting equity accounting (method 1) as adopted consolidated accounts

(method 6). Of particular significance in the context of this thesis is the fact that the equity method can be characterized as no more than a modification of legal entity-based accounts, given that it involves the practice of including profits and losses of subsidiary companies in the holding company's accounts.

Therefore, it seems possible to draw a tentative conclusion here that the adherence of holding company directors to the legal entity-based accounts which was shared by a number of them was institutionalised and thus made change occur slowly. This point will be dealt with more fully in chapter 9.

Chapter 6 The accountancy profession's attitudes 1 – Early literature on group accounting

6.1 Introduction

The purpose of this and the following two chapters (7 & 8) is to obtain an understanding of the accountancy profession's attitudes towards group accounting in the UK in the first half of twentieth century. As with the examination of group accounting practices (chapters 4 & 5), the focus will be on the equity method and consolidated accounts, i.e. methods 1 and 6. Selecting the accountancy profession's attitudes towards group accounting as a unit of analysis, in addition to holding company directors' group accounting practices, is the manner which is in accordance with the previous literature (see 1.3.2 of chapter 1). The main purpose of investigating the accountancy profession's attitude is to examine if it is possible to explain the holding company directors' group accounting practices from the viewpoint of the accountancy profession.

This chapter evaluates the content of eleven early books published in the UK between 1900 and 1929 stored in the ICAEW Library and seven articles which mostly appeared in *The Accountant*, also between 1900 and 1929. Of these 18 publications, 12 books/articles recommended the adoption of some form of group accounts. These 12 items were placed in three categories, reflecting their different attitudes or backgrounds. The first group covers those selecting the equity method as the appropriate method, the second group recognises the applicability of multiple solutions and the last group comprises 2 books/articles not written by British accountants. For the reason given below, these two items are considered not to represent 'the British accountancy profession's attitude'. Evidence of the ideas put forward by each group is presented in section 6.5 below.

Attention will also be drawn to the fact that 80.0% (=8/10) of the relevant literature proposed adoption of the equity method, i.e. the inclusion of profits and losses of subsidiary

companies in the holding company's statutory (legal entity-based) accounts irrespective of dividends actually declared or paid, as an appropriate method of group accounting during this period. The support provided for the equity method is further explored.

6.2 The Accountancy Profession investigated

The sources of insight considered to represent the attitude of the accountancy profession towards group accounting, employed in chapters 6-8, are not the same. This is because, during the different time periods covered by these chapters, different types of evidence are considered most significant given the subject of this thesis. Chapter 6 will investigate books and articles published by leading accountants and writers between 1900 and 1929. Chapter 7 will study the content of the 'Finance and Commerce' section of *The Accountant* between 1929 and 1948 for relevant insights, and Chapter 8 provides further illumination concerning the profession's attitudes during this latter period by presenting the results of a search through the ICAEW internal records for the period 1942-44. In other words, the opinion of the accountancy profession is seen to be principally represented by leading accountants and writers in Chapter 6, the contributors to the 'Finance and Commerce' section of *The Accountant* in Chapter 7 and the ICAEW leadership in Chapter 8. The reason for the different choices will be further explained in each chapter.

6.3 Sources of evidence investigated

In order to obtain an understanding of the accountancy profession's attitudes towards group accounting in the first half of twentieth century in the UK, this chapter will investigate books and articles published between 1900 and 1929. During this important formative period of

group accounting, the number of books and articles on the topic of group accounting was not enormous and it is considered possible to examine all available relevant material.

The books investigated in this chapter were identified through studying the ICAEW Library and Information Service Catalogue which can be accessed via the internet[58]. The database is called LibCat and is described as 'a single database with details of around 40,000 books, 30,000 journal articles and other items in the Library Collection' (The ICAEW Library and Information Service). The ICAEW library is highly regarded: in the Guildhall Library's words 'the Institute maintains a library containing a comprehensive collection of United Kingdom and world-wide accounting publications' (Guildhall Library Manuscripts Section's leaflet for 'Records of the Institute of Chartered Accountants in England and Wales and its Predecessor Bodies at Guildhall Library': 5).

6.4 Period investigated

The period selected for study in this chapter is from 1900 to 1929. It is considered appropriate to set the starting year for this chapter as 1900, because A.L. Dickinson's three papers, which are considered as 'the earliest clear writings on group accounting' (Walker, 1978: 148), were published between 1904 and 1906 (Dickinson, 1904; 1905; 1906). Dickinson was a British accountant and was practising in the US from 1901 to 1913 (DeMond, 1951; Edwards, 1984). His first paper (Dickinson, 1904), was presented at the International Congress of Accountants held at the World's Fair, St. Louis on 26th-28th September 1904. This paper was published in the official record of the Congress and, in the UK, in *The Incorporated Accountants' Journal* (November 1904, pp.34-40). The second (Dickinson, 1905) was a lecture given on 8th March 1905 before the School of Commerce, Accounts, and

[58] The URL is http://libcat.icaew.co.uk/uhtbin/cgisirsi.exe/U5m0CTim6e/0/0/49

Finance, New York University. The lecture was reprinted in the British journal *The Accountant* (7 October 1905, pp.402-410). Dickinson (1906) is a contribution to the initial volume of *The Journal of Accountancy* in America and a month later it appeared also in *The Accountant* in Britain (19 May 1906, pp.647-649).

The end date for this chapter is 1929, which is when the first Companies Act addressing the issue of how to account for the financial affairs of holding companies took effect. Books which were published *after* the CA29 naturally contained references and arguments concerning the legal provisions on group accounting, but books which were published *before* the CA29 are considered more likely to discuss the matter freely and without any regulatory-inspired constraint.

6.5 Literature search

6.5.1 Book survey

The ICAEW LibCat showed that 175 books were published with the word 'accounts' in their title between 1900 and 1929, 77 books with the word 'accounting' and 18 books with the word 'auditing' (Table 6-1). Among these 270 books, 225 books were published in the UK and the rest were published elsewhere in the world. According to the 'Subjects' classification devised by the ICAEW Library and Information Service, 68 books can be identified as relevant to this study, consisting of 50 books on book-keeping/accounting, 13 books on auditing and 5 books on trust/consolidation (Table 6-1).

Table 6-1 Numbers of books 1900-1929

Word in title	*accounts*	*accounting*	*auditing*	*total*
Number published	175	77	18	270
published in UK	161	48	16	225
published out of UK	14	29	2	45
Subject:				
book-keeping/accounting	24	25	1	
trust/consolidation	5			
Auditing			13	
cost/factory accounting	23	15		
Executor	22			
hospitals/schools accounting	13			
local government	11	2	1	
accountancy body's reports	9			
Income tax	6			
farming accounting	5			
industry-based	27	4		
Other	16	2	1	
Total	161	48	16	

Source: ICAEW Library and Information Service Catalogue

Of these 68 books, adjustment needed to be made for two books listed under two different subject areas[59], and one item which was merely an addendum to a book previously published[60]. Further, for the 12 titles which had multiple editions, only the latest (closest to 1929) version was retained on the list for inspection, and the other 31 editions were excluded[61]. After adding 6 more books which were discovered through searches of other

[59] Dicksee's *Advanced Accounting - with an appendix on the law relating to accounts* (5th ed. London: Gee, 1916) was picked up twice under subject titles of 'accounting' and 'accounts'. Johnson's *Book-keeping and Accounts, with Notes on Auditing, etc.* (London: Effingham Wilson, 1905) was also picked up twice under subject titles of 'accounts' and 'auditing'.

[60] Dicksee, L.R., *Auditing: Practical Manual for Auditors - Addendum*, London: Gee, 1929, 42p. Attached to Main Volume.

[61] The reason for retaining the latest (closest to 1929) version is that the revised versions are more likely to cover the topic of holding company accounts than earlier versions. The excluded editions are as follows: Chandler's *Trust Accounts* (2nd), Coles' *Company Accounts* (1st, 2nd), Cropper's *Book-keeping and accounts* (1st, 2nd, 11th, 12th), Cropper's *Accounting* (1st, 2nd), de Paula's *The Principles of Auditing* (1st), Dicksee's *Auditing* (9th, 10th, 11th, 12th, 14th), Fieldhouse's *The Students' Complete Commercial Book-keeping, Accounting and Banking* (9th, 11th, 12th, 14th, 15th, 20th, 34th), Fieldhouse's *The Students' Advanced Commercial Book-keeping, Accounting and Banking* (1st, 20th), Fieldhouse's *The Student's Elementary Commercial Book-keeping, Accounting and Banking* (13th), Mackay's *Company Accounting* (1911),

available catalogues (Ashworth, 1925b; Cutforth, 1923, 1926; Leake, 1923, 1929; Simons, 1927), the study sample contains 40 books on accounting, book-keeping, auditing and group accounts published between 1900 and 1929.

The texts of the 40 books were then examined to discover whether, and how, they dealt with the accounting practices of holding companies. Of the 40 books, 11 covered the issue of holding company accounts. Table 6-2 summarises the result of this exercise.

Spicer's *Practical Auditing* (2nd), Spicer's *Book-keeping and Accounts* (3rd, 4th, 5th, 6th). It is noted here that Dicksee's *Auditing* is exception and the version on the list is 13th edition rather than 14th. This is because the literature already reports that Dicksee included a chapter on holding companies beginning with the 13th edition in 1924 (Edwards and Webb, 1984: 35).

Table 6-2 Book survey 1900-1929

	author	title	year	Coverage of Holding Company Accounts
1	Ashworth, R.	*Limited Liability Companies*	1925	pp.188-191
2	BM/FAX 5 [pseud.]	*The ordinary man's own accounts*	1926	no
3	Carter, R.N.	*Advanced Accounts*	1925	pp.944-949
4	Chandler, P.W.	*Trust accounts*	1919	no
5	Chick, A.F.	*Apportionment in relation to trust accounts*	1923	N/A*
6	Coles, A.	*Company accounts*	1925	pp.293-295
7	Cropper, L.C.	*Book-keeping and accounts*	1927	no
8	Cropper, L.C.	*Higher book-keeping and accounts*	1927	no
9	Cropper, L.C.	*Key to book keeping and accounts*	1915	no
10	Cropper, L.C.	*Accounting*	1929	no**
11	Cutforth, A.E.	*Audits*	1923	no
12	Cutforth, A.E.	*Methods of Amalgamation*	1926	chapter VI
13	Davey, F.	*The students' catechism on book-keeping, accounting and banking*	1927	no
14	De Paula, F.R.M.	*The principles of auditing*	1928	pp.84-85
15	De, Zouche, R.C.	*Accounting*	1921	no
16	Dicksee, L.R.	*Advanced Accounting*	1916	no
17	Dicksee, L.R.	*How to install a proper accounting system*	1925	no
18	Dicksee, L.R.	*Auditing*	1924	pp.288-297
19	Fieldhouse, A.	*The students' advanced commercial book-keeping, accounting and banking*	1918	no
20	Fieldhouse, A.	*The student's elementary commercial book-keeping, accounting and banking*	1926	no
21	Fieldhouse, A.	*The students' complete commercial book-keeping, accounting and banking*	1929	no
22	Garnsey, G.	*Holding companies and their published accounts*	1923	chapter V-IX
23	Greenwood, W.J.	*Book-keeping and accounting exercises for accountant students*	1904	no
24	Greenwood, W.J.	*Book-keeping made easy*	1912	no
25	Hammond, E.J.	*Consignments, account sales and accounts current*	1924	no
26	Jackson, G.	*A practical system of book-keeping*	1902	no
27	Johnson, G.	*Book-keeping and accounts*	1905	no
28	Lancaster, J.	*Principles and practice of auditing*	1927	pp.165-166
29	Leake, P.D.	*Balance sheet Values*	1929	no
30	Leake, P.D.	*Depreciation and Wasting assets, and their treatment in assessing*	1923	no
31	Mackay, J.D.C.	*Company accounting*	1919	no
32	Merrett, H.C.	*Accounting and cost finding*	1924	no
33	Nixon, A.	*Manual of bookkeeping and accounting*	1921	no
34	Porritt, H.W.	*Pitman's higher book-keeping and accounts*	1911	no
35	Simons, A.J.	*Holding Companies*	1927	chapter V-X
36	Spicer, E.E.	*Practical auditing*	1919	no
37	Spicer, E.E.	*Book-keeping and accounts*	1927	no
38	Taylor, E.M.	*One hundred questions and answers in auditing*	1927	pp.89, 93, 106, 116
39	Vickery, B.G.	*Principles and practice of book-keeping and accounts*	1928	pp.294-295
40	Wardhaugh, J.B.	*Trust law and accounts*	1928	no

*The ICAEW librarian has been unable to find this item. It is unlikely, given the title, to contain material on holding companies accounts.

**Cropper (1929) added the provisions of the Companies Act of 1929, but it does not contain his own opinion/attitude towards group accounting and on this point the coverage was considered as "no".

Shaded rows identify the 11 books dealing with holding company accounts.

Source: original

6.5.2 Journal article survey

In order to achieve a fuller image of the accountancy profession's attitudes towards group accounting between 1900 and 1929, the journal *The Accountant* was also surveyed[62]. The indexes for the period 1900-1929 revealed 41 items that can be identified by using the following appropriate keywords: 'holding company', 'consolidated balance sheets', 'subsidiary (profits/losses)', and 'group accounts'. Table 6-3 shows the results.

Table 6-3 Items traced using the index to *The Accountant*, 1900-1929

	keywords				
	holding company	*consolidated B/S*	*subsidiary*	*group accounts*	*total*
lecture	3	2	0	0	5
leading article	5	5	0	0	10
weekly notes	4	5	2	0	11
correspondence	6	2	4	0	12
queries & replies	0	0	3	0	3
total	18	14	9	0	41

Source: *The Accountant*

From the 41 items above, only the 5 lectures (Cash, 1929; Garnsey, 1923, 1926; Stamp, 1925; Staub, 1929) were considered appropriate for further study since it is impossible to identify the authors of other items. Also, in the case of 'weekly notes' 'correspondence' and 'queries & replies', the items are usually too short to indicate the authors' attitude fully enough and, moreover, there are many cases where the author has not reached a conclusion on the matter of holding companies' accounts. Five more articles (Ashworth, 1925b; D'Arcy Cooper 1925; Garnsey, 1925; Leake, 1925; Whinney, 1925) published elsewhere, which were referred to in 'a leading article' in *The Accountant* (The Accounts of Holding Companies, *The Accountant*, 8 August 1925), and two more articles published in *The Accountant* (Kerr, 1915;

[62] Some reasons for surveying the journal will be provided in the next chapter (section 7.3).

Morgan, 1927[63]) but not revealed by the keyword search are added to the list. Dickinson's three papers (1904) (1905) (1906), which are known as the first clear writings on group accounting (Walker, 1978: 148), were not included on the list because it is likely that they dealt with American practices. Table 6-4 shows the result.

Table 6-4 Journal articles survey, 1900-1929

	author	*title*	*date*
1	Ashworth, R.	Consolidated Balance Sheets	5 Jun. 1925
2	Cash, William	Consolidated Balance Sheets	7 Dec. 1929
3	D'Arcy Cooper, F.	Consolidated Balance Sheets	3 Jun. 1925
4	Garnsey, G.	Holding Companies and their Published Accounts	6 & 13 Jan. 1923
5	Garnsey, G.	Consolidated Balance Sheets	29 May. 1925
6	Garnsey, G.	Holding Companies and their Published Accounts	20 Feb. 1926
7	Kerr, D.S.	Consolidated Balance Sheets	20 Nov. 1915
8	Leake, P.D.	Consolidated Balance Sheets	6 Jun. 1925
9	Morgan, H.	Published Balance Sheets and Accounts	25 Jun. 1927
10	Stamp, J.	Audit of "Holding " Companies	21 Feb. 1925
11	Staub. Walter A.	Consolidated Financial Statements	7 Dec. 1929
12	Whinney, A.	Consolidated Balance Sheets	3 Jun. 1925

Shaded rows identify the 7 articles written by authors who have not published books on the subject.

Source: original

Seven of the above authors (Cash, D'Arcy Cooper, Kerr, Morgan, Stamp, Staub and Whinney) had not written books on the subject. A comparison of the content of the other five articles reveals that the views expressed by their three authors (Ashworth, Garnsey and Leake) are consistent with that appearing in their books. Items in the former group only, therefore, were selected for analysis in the next section.

[63] These were picked up from Walker (1978:22, 79).

6.6 Findings from literature search

6.6.1 Group accounting theory as exemplified by the literature 1900-29

Table 6-5 is a list of the eleven books from Table 6-2 and the seven articles from Table 6-4 presented in a chronological order. Table 6-6 summarises the result of the survey of their contents. It identifies the preferred method(s) of group accounting by the 18 books/articles. It will be noted that all listed items, save Kerr, were published in the 1920s, with the first of those being Garnsey's celebrated text.

Table 6-5 List of literature investigated 1900-1929

	Author	*Title*	*Year*
1	Kerr, D.S.	*Consolidated balance sheets*	1915
2	Garnsey, G.	*Holding companies and their published accounts*	1923
3	Dicksee, L.R.	*Auditing*	1924
4	Ashworth, R	*Limited liability companies*	1925
5	Carter, R.N.	*Advanced accounts*	1925
6	Coles, A.	*Company accounts*	1925
7	D'Arcy Cooper, F.	*Consolidated balance sheets*	1925
8	Stamp, J.	*Audit of 'holding' companies*	1925
9	Whinney, A	*Consolidated balance sheets*	1925
10	Cutforth, A.E.	*Methods of amalgamation*	1926
11	Lancaster, J.	*Principles and practice of auditing*	1927
12	Simons, A.J.	*Holding companies*	1927
13	Taylor, E.M.	*One hundred questions and answers in auditing*	1927
14	Morgan, H.	*Published balance sheets and accounts*	1927
15	De Paula, F.R.M.	*The principles of auditing*	1928
16	Vickery, B.G.	*Principles and practice of book-keeping and accounts*	1928
17	Cash, W.	*Consolidated balance sheets*	1929
18	Staub, W. A.	*Consolidated financial statements*	1929

Source: Tables 6-2 and 6-4 of this chapter

Table 6-6 Accountants' Attitudes 1900-1929

		preferred method(s)			
method 1	method 2	method 3	method 4	method 5	method 6
Dicksee (1924)					
D'Arcy Cooper (1925)					
Morgan (1927)					
de Paula (1928)					
Cash (1929)					
Kerr (1915)	Kerr (1915)				Kerr (1915)
Garnsey (1923)	Garnsey (1923)	Garnsey (1923)			Garnsey (1923)
Simons (1927)	Simons (1927)	Simons (1927)			Simons (1927)
	Vickery (1928)	Vickery (1928)			Vickery (1928)
	Ashworth (1925)	Ashworth (1925)		Ashworth (1925)	
				Staub (1925)	
					Stamp (1925a)

Source: original

Six publications listed in Table 6-5 do not feature in Table 6-6 for the following reasons:

- Whinney, A. (1925), because the article did not recommend any form of group accounts but stated that 'the only balance sheet which a company is, by law, bound to issue is that which is required by implication by the Companies Consolidation Act, 1908, and by a company's articles of association'.
- Carter (1925: 944-949), Coles (1925: 293-295) and Cutforth (1926: chapter VI), because their coverage of holding company accounts related only to issues arising at the time of their formation.
- Lancaster (1927: 165-166), because the article did not recommend any form of group accounts but stated that 'the auditor has to rely upon his own examination of the balance sheets of the subsidiary companies and upon the rate of interest or dividend which has been received' (p.166).
- Taylor (1927: 89, 93, 106, 116), because the article did not recommend any form of group accounts but stated that 'the authors have dealt with this matter in works on *Accountancy*' (p.89). Unfortunately, the item on *Accountancy* could not be traced.

In Table 6-6, the remaining twelve publications are arranged according to what its author

proposes as the best method, or methods, of group accounting. For example, Dicksee (1924) proposed method 1 as the best group accounting practice. According to the patterns observed from the Table 6-6, there seem to be two types of conclusion on group accounting. One pattern revealed in those writings focuses on the issue of the equity method (method 1) as the appropriate solution (Dicksee, 1924; D'Arcy Cooper, 1925; Morgan, 1927; de Paula, 1928, Cash, 1929). The other pattern concerns those authors who acknowledge the existence of a number of acceptable ways of accounting for groups of companies and suggest no single method as most appropriate (Kerr, 1915; Garnsey, 1923; Simons, 1927; Vickery, 1928; Ashworth, 1925). Two items are considered exceptional (Staub, 1925; Stamp, 1925a), because of the reason stated below (sub-section 6.6.5). The two identifiable patterns will be fully discussed in sub-sections 6.6.3 and 6.6.4. Firstly, however, as context for those discussion, it is instructive to take a look at the background to the writings, *i.e.* the accounting problems of holding companies observed by the professional accountants of the day.

6.6.2 Problems recognised by contemporary professional accountants

The problems of holding company accounts were well recognised by the professional accountants in Britain, in the 1920s, in various ways. Some writers drew attention to the possibility that the profit and loss account of holding companies might sometimes be made up without providing for certain subsidiary companies' losses while, at the same time, absorbing other subsidiary companies' profits.

> ... it is believed that the omission on the part of some corporations to take up the losses of subsidiary companies, when they have included among their own earnings all the profits, has resulted in erroneous opinions as to the actual net earnings of the corporations in question.
>
> (Dicksee, 1924: 289)

> ... cases arose where it was claimed that a holding company could use dividends declared or profits earned by one or more subsidiary companies and simultaneously ignore trading

> losses incurred by others.
>
> (Cash, 1929: 641)

> He instanced a recent case of a company, C., which owned subsidiaries A. and B. A. made a considerable profit and B. made an almost equivalent loss, so that the concern, as a whole, had achieved no result warranting a dividend. Nevertheless, C. ignored the loss in B., had a full dividend from A., and used it to pay a dividend to its shareholders.
>
> (Stamp, 1925a: 312)

> In a case where some of the subsidiary companies are making large profits and others losses, the shareholders of the holding company may be seriously misled if no provision is made for depreciation of the shares held in the losing companies.
>
> (de Paula, 1928: 85)

Another problem recognised was that balance sheets of holding companies were deficient in that they contained no information about the assets and liabilities of subsidiaries and because loans and advances to subsidiary companies were often included among the holding company's assets.

> Frequently, the Balance Sheet of the holding company simply gives its own assets and liabilities, and these convey practically no information at all so far as the actual condition of the subsidiary companies is concerned. In many instances very large loans to underlying companies are included in the assets.
>
> (Dicksee, 1924: 289)

> ... there undoubtedly existed a strong and well-informed body of opinion which regarded as unsatisfactory the form of balance sheet of a holding company where no information was afforded as to the assets and liabilities of the subsidiary companies, particularly when, as in many cases, investments in subsidiary companies were included in total figures with other investments, and loans and advances to subsidiaries with other debtors to the parent company.
>
> (Cash, 1929: 641)

There were also criticisms of the practice of holding companies reporting as profit dividends paid by subsidiaries out of pre-acquisition profits and unrealized profits arising from inter-group sales.

> In another instance the parent company obtained a dividend from a subsidiary by drawing upon the 'carry-forward' of profits which had accumulated in the subsidiary prior to its

> acquisition by the parent, and which were, therefore, included in the assets purchased, the full cost of such assets (including the balance of profits) being capitalised in the parent balance sheet.
>
> (Stamp, 1925a: 312)

> ... such as the selling of goods from one constituent to another, and registering a profit in the selling company which was not really a profit to the whole concern until the second company had sold them, or the making and selling of plant by one company to the capital account of the other and similar inter-company transactions in which no profit really resulted for concerns as a whole.
>
> (Stamp, 1925a: 312)

In addition, concern was expressed about the fact that transactions might be undertaken that were in the interests of the holding company but detrimental to the subsidiaries' minority shareholders.

> ... while transactions carried through by any one or more of the subsidiary undertakings may be to the advantage of the consolidation as a whole, yet at the same time they may seriously affect the interests of the outside shareholders. In this connection such transactions as inter-company buying and selling should be fair to all, and not merely be in the interests of the Holding Company or the group as a whole. Similarly, a loan from one subsidiary company to another without security may be perfectly reasonable looking at the concerns as a whole, and yet may be quite unfair if there are outside shareholders.
>
> (Garnsey, 1923: 13)

> There is also the danger of oppressive treatment of minority shareholders where, for instance, a subsidiary company pays no dividends but the parent company takes credit for its share of the profits and obtains the funds by means of advances from the subsidiary, thus getting the full benefit of ownership without distributing any dividends to minority shareholders.
>
> (Garnsey, 1923: 14)

The above extracts indicate the diversity and extent of the problems which were discussed under the title of holding company accounts in Britain in 1920s. The ICAEW later (1943) classified the issues under the two headings: 'balance sheet problem' and 'profit and loss accounts problem', the former being 'as to the way in which the funds of the holding company group so far as invested in subsidiary companies are distributed over the several types of asset belonging to the group' and the latter relating to the situation where holding

companies' accounts fail to 'disclose the results of the group as a whole' (ICAEW, 1943: Head 10(B)(1)). However, during this period from 1900 to 1929, it was usual to set out the problems in a descriptive manner, without any classification and neat categorization,[64] which may be partly why writers, at the time, proposed various solutions in different ways.

The next sub-section introduces literature which supported the equity method as a solution, which is followed by a sub-section that deals with literature supporting multiple methods of group accounting. The rest of the literature investigated in this chapter will be then referred to in sub-section 6.6.5.

6.6.3 Assessment of the equity method

There were five publications (Dicksee, 1924; D'Arcy Cooper, 1925a; Morgan, 1927; de Paula, 1928; Cash 1929) investigated in this study which were found to be in support of the equity method as a possible solution to the problems of holding company accounts (Table 6-6). All these authors were leading accountants of the day. Lawrence Robert Dicksee (1864-1932) was 'the most prolific and influential of the early British writers on accounting and auditing

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[64] An exception is Morgan (1927: 981-2) who enumerated four cases of 'serious abuses and objections' such as:

> (1) That by bringing into the parent company's balance sheet the interests in subsidiary companies at cost, losses have been undisclosed and disregarded in arriving at the amount of profits shown as available for payment of dividends.
> (2) That the parent company may take credit for unreal profits arising from the carrying out of contracts for the supply of goods to a subsidiary company at substantial profits when such contracts or goods so far as the subsidiary is concerned may be expenditure on capital account, or, if purchased for the purposes of trading, may be still on hand and unrealised at the date of the balance sheet.
> (3) That the object may be to provide for undisclosed increase of remuneration to directors of the parent company, who may be appointed as directors of the subsidiary companies, the directors' fees of which are frequently by no means unsubstantial.
> (4) To conceal excessive payments for goodwill or profits on purchase of a business; investments in other companies that may not be authorised by the holding company's memorandum and articles of association, or loans to directors or officers.

(Morgan, 1927: 981)

However, the literature did not develop the discussion of holding company accounts based on Morgan's classification.

and the first professor of accounting in a British university'[65] (Parker, 1984: 59). Frederic Rudolph Mackley de Paula (1882-1954) was 'the most influential British writer on accounting in the 1930s and 1940s,' (Parker, 1984: 55). de Paula 'succeeded Dicksee as part-time professor of accounting at the London School of Economics in 1926 but resigned in 1929 when he joined the Dunlop Rubber Co.'[66] (Parker, 1984: 56). Francis D'Arcy Cooper (1882-1941) was a son of Francis Cooper, partner in the accounting firm Cooper Brothers & Co. and a chairman of Lever Brothers and Unilever[67]. William Cash was a 'president of the ICAEW, 1921-3' (Matthews, Anderson and Edwards, 1998: 126) and Henry Morgan was a 'vice president of the SIAA' at the time (*The Incorporated Accountants' Journal*, May, 1927: 276). The range of arguments they put forward in support of the equity method is now illustrated.

Dicksee (1924: 293-294) advanced the following method for applying the equity method which equates to present-day practice.

> Where the [undistributed] earnings of subsidiary companies have been carried into the books of the holding company, it follows, of course, that either some asset account, such as that representing the investment in the subsidiary company, has been correspondingly increased, or else it will be debited to an account called 'Profits of Subsidiary Companies' and the holding company's current Profit and Loss Account credited. Following out the same line, where a loss has been made, the Investment Account (or any other account which represents the cost of the underlying property), or the accounts 'Profits of Subsidiary Companies,' should be correspondingly decreased and the current Profit and Loss Account of the holding company debited.
>
> (Dicksee, 1924: 293)

This requirement to recognise only the holding company's share of the subsidiary company's profits is explained as follows:

> The only legitimate way by which the holding company can secure its proportion of this profit being through dividends, it follows, of course, that the minority interests, no matter how small, will receive their share, although they can never be depended upon to contribute any proportion whatever of the losses.
>
> (Dicksee, 1924: 294)

65 For his biography, see Kitchen and Parker (1984: 51-63).
66 For his biography, see Kitchen and Parker (1984: 81-120).
67 For his biography, see Edwards, (1984a: 781-785).

Dicksee's recommendation for a more prudent approach towards the recognition of losses, however, is also explained.

> It is quite correct that its proportion of profits, only, should be taken up, but in many cases a holding company owning, say, ninety per cent. of the stock of another company, which is being operated by it in connection with other companies, should take up all the loss of the latter rather than its proportion only, which in this case would be ninety per cent. The reason for this is obvious. If the subsidiary company is an important or necessary link in the group usually operated by holding companies, and is losing money in its operations, it almost invariably happens that the parent company will be compelled to make cash advances sufficient to cover the losses sustained.
>
> (Dicksee, 1924: 292-293)

D'Arcy Cooper (1925a) clearly supported the equity method, including recognition of subsidiary companies' losses as well as profits.

> I do not think it would be denied that it would be improper for a parent company to take to the credit of its profit and loss account the profits of its subsidiary companies without reserving for losses of subsidiary companies.
>
> (D'Arcy Cooper, 1925a: 18)

D'Arcy Cooper underlined his support for the equity method when emphasising his opposition to publication of the consolidated balance sheet.

> ... but so long as this is done and the profit and loss account shows the total net profits or losses (as the case may be) of the whole of the companies, I see no useful purpose in producing an amalgamated balance-sheet which would be neither fish, flesh, fowl, nor good red herring.
>
> (D'Arcy Cooper, 1925a: 18)

Morgan presented the case for adopting the equity method as follows:

> In the majority of cases the position of a subsidiary in relation to the parent company is to all intents and purposes analogous to a branch of the main business, and I therefore maintain that, as regards the balance sheet of the parent company, the results of the subsidiary should be taken into account and dealt with in the same way as you would deal with the accounts of a branch ...
>
> (Morgan, 1927: 981)

The auditor's responsibility to ensure such aggregate profits and losses reflected in holding company accounts was also emphasised.

> I maintain that unless such aggregate profits and losses have been fully brought into the accounts of the holding company, not only has a shareholder a right to know that they have not been brought in, but he is also entitled to know the amount involved in such omission, and frankly, I cannot imagine that any reputable accountant could conscientiously sign a certificate that a holding company's balance sheet showed a true and correct view of the state of the company's affairs unless such aggregate profits or losses were taken into account.
>
> (Morgan, 1927: 982)

Whereas those above unequivocally favour use of the equity method, this is not the case with the next two. It is difficult to assume that the next two cases provide evidential support for the equity method by the writers of the day. However, they are presented here because they both talk about the inclusion of profits and losses of subsidiary companies in the holding company's statutory accounts (legal entity-based accounts), rather than introducing additional accounts such as consolidated accounts, as a means of tackling the problems that arose from the growing tendency of companies to carry on part of their business through subsidiaries. The difference between the former three publications (Dicksee, 1924; D'Arcy Cooper, 1925a; Morgan, 1927) and the latter two (de Paula, 1928; Cash, 1929) should be kept in mind.

de Paula (1928: 84-5) did not favour adoption of the equity method, in the sense of recognising undistributed profits generated by subsidiary companies, but he did advocate the importance of making provision on the balance sheet of the holding company for the losses incurred by their subsidiaries. In other words, de Paula supported the historical cost and prudence concepts as the bases for valuing subsidiaries.

> If the present financial position of a subsidiary company is equal to or stronger than it was at the time when the shares were acquired, then the shares held should appear in the holding company's Balance Sheet at cost. But if the financial position has changed for the worse by reason of losses incurred by the subsidiary company since the shares were acquired, then the value of the shares held should be reduced by the amount of such losses, this sum being written off to Profit and Loss Account, and thus set off against the income received from the successful companies.
>
> (de Paula, 1928: 85)

Cash was appointed to the Greene Committee and, some time after the Committee's report had been issued, he reflected on the treatment of subsidiaries in the accounts of holding companies. It seems that he had not been fully convinced of the case in support of equity accounting, but it is possible to see from his comments that he was aware of the fact that this was a method that some 'large and important' companies employed.

> The method at present followed, speaking generally, in the case of the largest combined Undertakings by Holding Companies is ... to bring in the Dividends declared or accrued in respect of Investments in the subsidiary Companies for the financial period and to state these in an aggregate sum with the Trading profit (if any) of the Holding Company.
>
> Instances of large and important Undertakings can be adduced where this latter procedure has been extended so as to bring in to the accounts of the Holding Company the profits of the subsidiary Companies and not only dividends declared.
>
> (Cash, 1929: 641-2)

Cash's contention was that the Greene Committee's recommendation represented best practice and that emphasis should be on the legal balance sheet.

> I think I may therefore state that the view and practice in England tends to adopt the principle of adherence to what we term the legal balance sheet, but to the disclosure therein under separate heads of the position between the parent or holding company and its subsidiaries ...
>
> (Cash, 1929: 644)

Cash and de Paula, people who then and/or later figured prominently in the leadership of the ICAEW, therefore favoured an approach where financial reports focused on holding companies as separate legal entities reporting their legal relationships with subsidiaries but, in accordance with the concept of conservatism, providing for all foreseeable losses.

6.6.4 Preference for multiple solutions

Five publications (Kerr, 1915; Garnsey, 1923; Simons 1927; Vickery, 1928; Ashworth, 1925) investigated in this study supported multiple solutions to the problem of how to account for subsidiaries (Table 6-6). Kerr (1915) is the earliest published literature among those listed

on Table 6-5. He proposed three methods, including the equity method as seen in the following paragraph.

> It is important that the accounts show the value of the equities of the stockholders of the holding company after taking into account all of the results of the changes in the assets and the liabilities of all of the subsidiary companies, thereby disclosing fully any increase (due to earnings) or decrease (due to losses) in the value of the combined equities in the various interests owned by the stockholders of the holding company.
>
> (Kerr, 1915: 629)

Kerr also supported the publication of consolidated accounts (method 6) or the balance sheets of subsidiaries in addition to the holding company's accounts (method 2). The publication of consolidated accounts is supported because

> As regards the practical business result, it is the same, so far as the operations of the consolidated plants are concerned, whether the consolidation be brought about by actual transfer of the assets, or by the acquiring of the capital stocks of the subsidiary companies...
>
> (Kerr, 1915: 627)

The circumstances in which 'the Balance Sheets of the individual subsidiary companies should be published' is also explained.

> ... where a holding company owns not all but a majority of the capital stock of a subsidiary company and the public own the balance of the stock, or where preferred stock of a subsidiary company is held by the public, it is important that these other stockholders should have periodical statements of the affairs of the subsidiary companies. Further, where subsidiary companies have outstanding bond issues, it is frequently very advisable to publish the individual Balance Sheets for the benefit of the bondholders.
>
> (Kerr, 1915: 627)

In his famous lecture delivered seven years later[68], Garnsey (1923) acknowledged four methods of group accounting, including the equity method but he described it as 'unusual'[69].

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[68] Kitchen (1972: 114) described the lecture that 'It is beyond doubt that the Garnsey lecture of 1922 was central to the development of accounting for holding company groups'.

[69] The equity method was criticised because it allows full recognition of profit earned by subsidiary companies which is not transferred to the holding company as dividends.

> When profits are taken up by the holding company which have not been declared as dividends by subsidiaries, it should be borne in mind that these are not available for the purpose of a dividend payable by the holding company. It is not desirable that such profits should be taken credit for, but

(1) To publish only the Holding Company's Balance Sheet and Profit and Loss Account, treating the interest in subsidiary companies as an investment in the Balance Sheet and including in the profits the dividends actually received from the subsidiary undertakings. The total profits and losses of the subsidiary undertakings are sometimes taken up in the Holding Company's Balance Sheet and Profit and Loss Account irrespective of what dividends are actually declared and paid, but this practice is unusual.
(2) To publish the Balance Sheet and Profit and Loss Account of the Holding Company as in (1) and to present simultaneously either the separate Balance Sheets and Profit and Loss Accounts of all the subsidiary companies; or
(3) As a separate Statement a summary of the assets and liabilities of all the subsidiary undertakings taken together.
(4) To publish either separately or along with the Holding Company's Balance Sheet (as in (1)) a consolidated Balance Sheet of the whole undertaking amalgamating the assets and liabilities of all the subsidiaries with those of the Holding Company and a consolidated Profit and Loss Account embracing the profits and losses of all the companies.

(Garnsey, 1923: 16)

Later in his paper, Garnsey (1923: 36) repeated his opinion that the equity method was 'seldom' used in Britain. However, he considered such treatment acceptable provided it is accompanied by appropriate disclosure. Indeed, just three years later he cited the method as both popular and a possible stepping-stone towards the adoption of consolidated accounts.

> It should be noticed that the practice adopted by many holding companies of taking up all profits and providing for all losses implies a Consolidated Profit and Loss Account and regards all the concerns as one entity. It would seem a logical development of that step to give a Consolidated Balance Sheet of the whole undertaking.
>
> (Garnsey, 1926: 272)

The following extract is also of interest because Garnsey focuses on the concept of control, not merely ownership, as a precondition for profit recognition.

> It might be that the directors would wish to take up any undistributed profits of subsidiaries as an asset in the Holding Company's Balance Sheet and credit the amount to the Profit and Loss Account. If, as is assumed, the undertakings are not merely owned but effectively controlled, and the amount is properly disclosed on the face of the accounts, then no objection could be raised to this course provided always that any losses of other subsidiaries are reserved for.
>
> (Garnsey, 1923: 36)

---

where they are so treated it is advisable to state the amount separately.
(Garnsey, 1926: 271)

In common with de Paula (1928), Garnsey (1923: 38-9) insisted that any losses incurred by the subsidiary companies should be provided for in full, rather than in proportion, by the holding company.

Simons (1927: 54) acknowledged the use by holding companies of four methods of group accounting, and considered each 'of especial value in particular cases' (Simons, 1927: 54). The four methods are, in essence the same as those acknowledged by Garnsey. However, Simons is more positive about the equity method than Garnsey, since he stated as follows:

> A better suggestion appears to be to value Investments in Subsidiaries at –
>
> Cost ± subsequent profits/losses – dividends declared out of surpluses existing at the date of acquisition
>
> (Simons, 1927: 68)

Ashworth (1925a) and Vickery (1928: 295) each acknowledged the utility of three methods of group accounting. Ashworth (1925a: 190-1) made his opinion clear that method 5 was the most appropriate, by commenting that method 2 'might be too expensive to adopt, and also the average shareholder would not have the necessary knowledge to enable him to amalgamate the results' and that method 5 'has the advantage of showing quite clearly the relation of the assets and liabilities of the companies as a whole to the capital of the parent company, and the capital held in the subsidiaries by persons other than the parent company'.

6.6.5 Other contributions

Staub (1925) supported method 5 (presenting consolidated balance sheet instead of the holding company's legal entity-based accounts) and, although Stamp (1925a) proposed the adoption of method 6 (consolidated accounts together with legal entity-based accounts), he considered method 5 more desirable. Staub, an American, was a member of the New York State Society of Certified Public Accountants. Stamp (1925a: 312) contrasts British practice

with that in America and concludes 'that the science of making consolidated accounts had not advanced far in this country, though it was well known in America'. Although favouring the US procedure of publishing only a consolidated balance sheet (method 5), he admitted that 'Doubtless the day was not yet very near when such statements could be appropriately presented in place of the present form, but as auxiliary means of exposing the facts [method 6] they were invaluable' (Stamp, 1925a: 312).

Those two cases therefore promoted the adoption of either method 5 or method 6. However, on the ground that Staub was an American accountant and that Stamp was not an accountant[70], it is considered in this study that the third attitude (sub-section 6.6.5) does not represent British accountancy profession's attitudes towards group accounting during the period from 1900 to 1929.

6.7 Consistency with previous literature

It was seen above that there were two attitudes, concerning the adoption of group accounting, expressed by members of the British accountancy profession from 1900 to 1929. One pattern of thought was in support of the equity method (sub-section 6.6.2) and the other was an acknowledgement of the existence of a number of acceptable ways of accounting for groups of companies (sub-section 6.6.3). There were five books/articles which supported a range of possible solutions, of which three proposed the equity method as one of the alternatives. Adding the three items to those of the first attitude, there totalled eight books/articles supporting the equity method, i.e. the amendment of holding company's accounts by including profits and losses of subsidiary companies irrespective of dividends actually declared or paid. In other words, of all books/articles investigated in this study,

[70] For the biography of Josiah Charles Stamp (1880-1941), see Beveridge (1959) and Bywater (1984).

80.0% (=8/10) of the relevant publications which covered the topic of group accounting proposed the equity method as an appropriate method during this period. Even if excluding three items (de Paula, 1928; Cash, 1929; Garnsey, 1923), as they did not clearly recommend inclusion of profits of subsidiary companies, half of the writings were positive about the equity method.

This finding is an important contribution of this study, since no previous literature has revealed the point that the equity method was the popular group accounting method among the British accountancy profession between 1900 and 1929. However, when turning an eye to influential individual accountants at that time, it can be noticed that there is some important consistency with previous literature. In this section, three British accountants (A.L. Dickinson, L.R. Dicksee and F. D'Arcy Cooper) who supported the equity method will be focused on, and their influence which has been described in previous literature will be observed.

6.7.1 Influence of Dickinson

Accounting historians (for example, see Parker, 1984; Kitchen and Parker, 1984) agree that Dicksee's *Auditing: Practical Manual for Auditors* was a famous and influential textbook at the time, but, before focusing upon Dicksee, this sub-section will pay attention to Dickinson[71]. This is because a large part of the chapter on group accounting in Dicksee's *Auditing* consists of extracts from Dickinson (1904). Dicksee defers to Dickinson when saying that 'the opinion of A. Lowes Dickinson, F.C.A., C.P.A., on this subject, as reflected in his paper, read at the St. Louis Congress of Accountants, is of importance, as it is believed that the view there

[71] Arthur Lowes Dickinson (1859-1935) was a British accountant but practised for some time in America. He and William J. Filbert of US Steel together produced the accounts of US Steel for 1902, which contain the best-known early example of a consolidated statement, and the accounts attracted widespread acclaim as a breakthrough towards full and meaningful financial disclosure (Edwards, 1984b: 104). Dickinson returned to Britain in 1913 and remained a partner in the London office of Price, Waterhouse until his retirement in 1923 (Edwards, 1984b: 104). He was a member of the ICAEW's council, 1914-28, and maintained an active involvement in professional developments (Edwards, 1984b: 104).

expressed represents the best accountancy practice' (Dicksee, 1924: 290). Dickinson must have been talking about the US practice, but Dicksee paid particular attention to his discussion.

Amongst the extracted paragraphs from Dickinson (1904), two powerful, modern arguments in support of the equity method are presented. First, the need to remove opportunities from managements to abuse their discretion was noted.

> If this principle [equity accounting] be not insisted upon, it is within the power of the directors of the holding company to regulate its Profits according not to facts, but to their own wishes, by distributing or withholding dividends of the subsidiary companies; or even to largely overstate the Profits of the whole group by declaring large dividends in those sub-companies which have made Profits, while entirely omitting to make provision for Losses which have been made by other companies in the group.
>
> (Dickinson, 1904: 189-190)

Second, the need for published financial reports to reflect changes in values was stated.

> It is doubtful whether there is any existing law which could legally require a corporation to make up its Statement of Profits on the basis here suggested, but possibly it may eventually be found that the ordinary rule referred to at the commencement of this paper, of a reasonable valuation of Assets, may be made to cover this point for the following reasons:
>
> ... On general principle, therefore, that a Profit and Loss Account should take into account all Profits or Losses resulting from the trading operations, but should not take into account the Profits or Losses arising from a revaluation of Capital Assets, it may eventually be held, on legal as well as on accounting principles, that the Statement of Earnings presented by a holding company is not correct unless it takes into account by way of either a reserve or a direct addition to or deduction from the capital value of the investment the Profits or Losses made in operating the subsidiary companies.
>
> (Dickinson, 1904: 190)

Of key importance for this thesis is the fact that Dicksee chose to quote neither Dickinson (1905) nor Dickinson (1906), but instead reproduced substantial extracts from Dickinson (1904). As mentioned earlier in this chapter, Dickinson wrote three papers which are considered today as the earliest clear writings on group accounting (Dickinson, 1904, 1905, 1906). It was also mentioned that all of the three papers were reprinted in British journals in

the same years. In other words, the three papers were easily accessible to British accountants of the day. It can be well assumed that Dicksee was acquainted with all the three papers. Dicksee's decision to quote from Dickinson (1904) can be considered as an intentional choice.

Dickinson (1905, 1906) explicitly favoured the consolidation method of group accounting, whereas this was not the case in Dickinson (1904)[72]. Dicksee did not state why he had chosen to reproduce extracts only from Dickinson (1904). However, the fact that Dicksee quoted Dickinson (1904) and that he neglected to cite either of Dickinson's two other papers can be said to indicate Dicksee's attitude towards group accounting very clearly.

The historical importance of Dickinson's 1904 paper is recorded by Edwards (1984b) as follows:

> He [Dickinson] was heavily involved in arranging the 1904 International Congress on Accounting, and the paper which he read, entitled 'Profits of a Corporation', was a major contribution to the academic success of that meeting. (Edwards, 1984b: 104)

The fact that Dickinson was an influential figure amongst the accountancy profession of the day, is likely to have explained why Dicksee chose to quote his publication as authoritative support for the equity method which he, himself, favoured.

6.7.2 Influence of Dicksee

It is important to the arguments presented in this thesis that Dicksee was also a highly influential figure. Kitchen and Parker (1984: 63) stated that 'In his day, Lawrence Dicksee's contribution to education and ideas in accounting was an enormous one'. Dicksee was 'the most prolific and influential of the early British writers on accounting (as distinct from bookkeeping) and auditing and the first professor of accounting (part-time) in a British

[72] No evidence was found which explains why Dickinson changed his mind from supporting the equity method in 1904 to favouring consolidated accounts in 1905 and 1906. It could be argued, however, that Dickinson became less preoccupied with his British background and became able to ignore the legal basis of financial reporting when he wrote papers in 1905 and 1906.

university' (Parker, 1984: 59). His *Auditing: Practical Manual for Auditors* was widely used by students and practitioners and highly respected. 'Fourteen British editions were published during Dicksee's lifetime, the fifteenth was in preparation when he died', and 'the book found a market also in the United States' (Kitchen and Parker, 1984: 57-8). The fact that what Dicksee said in his *Auditing* carried a lot of weight may be a reason which explains the support for the equity method by other accountants and writers.

Dicksee wrote a section on group accounting in the American version much earlier than in the British version of his text. As Edwards and Webb (1984: 35) noted, it is known that Dicksee's *Auditing* contained a section of group accounting beginning with the 13th edition in 1924. However, when turning an eye to the American edition of *Auditing*, he dealt with the topic commencing with the 2nd American edition in 1909. The sentences were almost the same. In other words, as early as in 1909, Dicksee had already decided his attitude towards group accounting[73]. At the time of publishing the 13th edition of his book in Britain, he already had fifteen years in which to develop his ideas.

It is also probably relevant to note that Dicksee's 13th British edition was published almost immediately after Garnsey's lecture given to the London members of the ICAEW. Indeed Dicksee specifically referred to the lecture as follows:

> More recently the subject of Holding Companies and their Published Accounts has been dealt with by Sir Gilbert Garnsey, K.B.E., F.C.A., in a paper read by him before the London members of the Institute of Chartered Accountants on 1st December 1922, a full report of which appeared in The Accountant of 6th and 13th January 1923.
>
> (Dicksee, 1924: 295)

It could be possible to imagine that Dicksee's insertion of a group accounting section in the 1924 edition of his book was in response to Garnsey's lecture having raised the profile of the

[73] The American versions of *Auditing* was edited by Robert H. Montgomery, but Dicksee authorised that 'it has been issued by arrangement with me, and that the various alterations and amendments that have been effected, with a view to making the work more suitable to the needs of American practitioners and accountant students, have all been submitted to me and have met with my entire approval' (Dicksee, 1909: 4).

subject in Britain. Dicksee acknowledged the lecture in his book as an event that had taken place, but he did not further introduce Garnsey's discussion. Instead, he reprinted extracts from the American edition of his book. Dicksee's decision to promote the equity method is perhaps indicative of the fact that, given the amount of time he had reflected on these issues, he had much confidence in the validity of the particular conclusion he had reached.

6.7.3 Influence of D'Arcy Cooper

The important role played by D'Arcy Cooper, who had considerable experience as an auditor of large companies before joining top management at Lever Brothers, in the 1920s is today described as follows:

> Cooper's letters written to the Times (3 June 1925) and the Greene Committee (24 June 1925), and verbal evidence given before the Greene Committee, strongly opposed the view, favoured by many accountants, that companies should be legally required to publish consolidated accounts. ... it is likely that Cooper's arguments helped delay, until 1948, the introduction of a legal requirement for companies to publish group accounts. (Edwards, 1984a: 784)

Lever Brothers, of which D'Arcy Cooper was the chairman from 1925, was known as a famous user of the equity method. Simons reprinted the company's Balance Sheet in his book (Simons, 1927: 164). Much more recently, Camfferman and Zeff (2003: 186) reported that there was 'the long-held belief within Unilever that consolidated balance sheets would be misleading'.

There seems no doubt that D'Arcy Cooper's view was influential at the time. His confidence in what he proposed can be inferred from the following public statements criticizing the publication of consolidated accounts and supporting the use of the equity method. In an article in the leading contemporary British newspaper, *The Times*:

> I see no useful purpose in producing an amalgamated balance sheet which would be neither fish, flesh, fowl, nor good red herring. On the contrary, in my opinion it could only do harm.
>
> (D'Arcy Cooper, 1925a: 18)

In evidence presented to the Greene Committee:

> I strongly support the present practice of holding Companies which is to take to the credit of Profit and Loss Account either the dividends declared or the profits earned by subsidiary Companies, whilst at the same time providing out of the holding Company's profits for all losses made by subsidiary Companies, and any legislation which may be necessary to enforce such a practice would, in my opinion, be sound and wise.
>
> (D'Arcy Cooper, 1925b: lx)

> Take one simple illustration:-
> A trading company forms a subsidiary company to undertake its transport work, that is to say, the collection and delivery of raw materials and the despatch and distribution of its finished products. It would be manifestly unfair to compel the publication of figures relating to the operations of that subsidiary company which, in effect, are part of the operations of the business as a whole and are divided, only for convenience in working and in keeping detailed accounts, from the parent company by means of the separate entity of a subsidiary company. What the shareholders in the business are concerned with are the results of the combined operations in the form of the Profit and Loss Account of the parent company.
>
> (D'Arcy Cooper, 1925b: lxi)

6.8 Conclusion

This chapter evaluates the significance for this study of group accounting of the content of books published in the UK between 1900 and 1929 and articles which mostly appeared in *The Accountant* also between 1900 and 1929. It was found that there were two elements in the British accountancy profession's attitudes towards group accounting. One pattern revealed in those writings focuses on the issue of the equity method (method 1) as the appropriate solution. The other pattern concerns those authors who acknowledge the existence of a number of acceptable ways of accounting for groups of companies and suggest no single method as most appropriate. There were five books/articles which favoured a range of possible solutions, of which three proposed the equity method as one of the alternatives. In other words, the equity method was proposed as an appropriate solution to the accounting problems of holding companies by most of the early literature.

This point has not been revealed by the previous literature, and can be considered to be an important contribution of this study. However, there is some important consistency with the previous literature in that it is already known that A.L. Dickinson, L.R. Dicksee and F. D'Arcy Cooper exerted a strong influence upon the British accountancy at that time. Dickinson, Dicksee and D'Arcy Cooper all documented their support for the equity method.

It seems possible to say that the preference for the equity method by the early literature on group accounting and by prominent accountants of the day provides a plausible explanation for the finding 3 of the previous chapter, i.e. the use of the equity method by a fairly constant percentage (13% or so) of holding company directors. This point will be further dealt with in chapter 9.

Chapter 7 The Accountancy Profession's Attitudes 2 – Finance and Commerce section, *The Accountant*

7.1 Introduction

This is the second chapter of the three which aim at obtaining an understanding of the accountancy profession's attitudes towards group accounting in the UK in the first half of twentieth century. This chapter focuses on the period between 1929 and 1948 and examines the contents of the influential and highly regarded journal *The Accountant*. In the Finance and Commerce section, *The Accountant* typically reproduced extracts from actual company accounts, fully or partly, and made positive or negative comments on their content. There are 1,043 issues during the period, and the investigation of the comments throughout the period is considered to provide a good source for obtaining an understanding of the accountancy profession's attitudes towards group accounting.

It will be shown that *The Accountant* paid extensive attention to group accounting practices throughout the period from 1929 to 1948. This is strong evidence to suggest that the accountancy profession was keenly interested in the matter in those days. Another finding will be that particular attention was paid to consolidated accounts, whereas the other group accounting methods were little commented on. In addition, it will be revealed that the accountancy profession, represented by *The Accountant*, did not reach a firm decision, until the issue of RoAP7, concerning which of the available group accounting practices was the best method to adopt.

7.2 Source of material investigated

The Accountant was first published in 1874 as 'a medium of communication between accountants in all parts of the United Kingdom' (the subtitle of the journal for the first issue).

As the above subtitle shows, it was not intended to be the mouthpiece for any particular professional body and it came to be described as 'the recognised weekly organ of chartered accountants and accountancy throughout the world' (the front page of issues during the period of this chapter). Moreover, *The Accountant* is possibly the premier British accounting journal of the first half of the twentieth century, and one widely used by accounting historians to achieve an understanding of contemporary theory and practice. For example, Stacey (1954: 23) described it as 'the recognized organ of chartered accountants to this day and the oldest accountancy journal in the world' and is said to be 'the greatest influence in British reporting practices' (Walker, 1978: 81). Brief described his delight on discovering the historical potential of a British journal, *The Accountant*, which he found on the shelves of the AICPA library:

> *The Accountant*, in particular, was a gold mine of information about the history of accounting and, in those days, the complete set, was immediately available. What a treasure! (Brief, 1993: xii)

Accordingly, an analysis of the content of *The Accountant* is considered appropriate for the purpose of building an understanding of what practices part of the 'establishment' within the British accountancy profession considered appropriate to recommend for wider adoption by British companies, or to discourage.

The reason for changing the source of material to investigate from that examined in chapter 6 is as follows. In chapter 6, all books from the database of the ICAEW LibCat, which were published in the UK between 1900 and 1929 with any word from 'accounts', 'accounting' or 'auditing' in their title and classified as 'bookkeeping/accounting', 'trust/consolidation' or 'auditing', were the main material to investigate. The period between 1900 and 1929 was when no regulations and few key events concerning group

accounting took place[74]. Also, as chapter 4 reveals, it was a time when relatively few companies published group accounts. On the other hand, during the period from 1929 to 1948, there occurred several important events for the development of group accounting in the UK, as introduced in chapter 2, such as Royal Mail case in 1931, Dunlop Rubber's accounts of 1933, RoAP 7 in 1944 and the CA48 in 1948. Accordingly, the latter period experienced more stimuli for change than the former period. It seems important then to observe when and how change, if any, has taken place, in order to identify which of the above events were more influential. For the period 1929-48, it is more practical and perhaps useful to look at one specific source of data, rather than to attempt to examine all available publications. By limiting the focus to an influential source, *The Accountant*, and by examining the change, if any, in the content of the journal throughout the period, it will be possible to achieve a more detailed and systematic analysis. At the same time, it should be pointed out that this approach is possible only when the issue of holding company accounts was dealt with in the journal frequently and repeatedly, which was not the case for the time period covered in chapter 6.

Moreover, it can be noted that the focus on *The Accountant* rather than textbooks is justified because in some cases at least the statements in textbooks started to repeat only the regulatory requirements when CA29 came into force. For example, the 15th edition of Dicksee's *Auditing*, published in 1933 after his death and edited by S. W. Rowland, contained completely different statement from that of 14th edition which was published before his death for the subject of accounts of holding companies (pp.322-4) which reflected the provisions of CA29.

The content of *The Accountant* usually consists of leading articles (by unknown authors), lectures (by professional accountants and other people of the day), weekly notes,

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[74] An exception was, of course, Garnsey's lecture in 1922, which is well known by accounting historians today as, for example, Kitchen (1972: 114) stated that 'it is beyond doubt that the Garnsey lecture of 1922 was central to the development of accounting for holding company groups'.

correspondence, queries & replies and so on. This chapter investigates the section entitled Finance and Commerce. In the section, *The Accountant* typically reproduced extracts from actual company accounts, fully or partly, and made positive or negative comments on their content. About 5 to 7 cases often appeared in a single issue. This section was a regular feature of volumes published during the period examined (from 1929 to 1948). The journal was, and still is, published every week, and there were 1,043 issues[75] from the start of 1929 to the end of 1948.

Thus the accountancy profession represented in this chapter is exemplified as the writers of Finance and Commerce section of *The Accountant*. Therefore it is noted that the word 'profession' is not used as specific professional bodies.

7.3 Periods investigated

The starting year for investigation, 1929, is when the first Companies Act addressing the issue of how to account for the financial affairs of holding companies took effect and chapter 6 was terminated. The end date for this chapter is 1948, which is when the CA48 required a holding company to publish the group accounts which were normally expected to be in the form of consolidated accounts comprising a consolidated balance sheet and a consolidated profit and loss statement.

[75] The section was omitted in 4 May 1946, 29 June 1946, 13 July 1946 and 17 May 1947 (No explanation for this was found in the journal.) Consequently, although there are 52 issues of *The Accountant* in each of the years 1946 and 1947, the Finance & Commerce section appeared 49 times in 1946 and 51 times in 1947. The frequency of comments on group accounting practices in the Finance & Commerce section was calculated based on the number of 52 in both 1946 and 1947 (Table 7-1) rather than 49 and 51, because it is considered that, for the readers of the journal, the two situations (no comments on group accounts in the section and no appearance of the section) are the same in that both provide no examples and comments on group accounts from writers of the section.

7.4 Findings

7.4.1 Extensive attention to group accounting

Table 7-1 shows the frequency with which comments concerning group accounts appeared in the Finance and Commerce section of *The Accountant* between 1929 and 1948. For the purpose of analysis there are picked up, not only those comments which were titled with such words as 'holding company', 'consolidated accounts', 'subsidiary companies' and 'group', but also any other comments which embraced issues related to group accounting practices[76]. The actual examples of the comments will be presented in sub-sections 7.4.2 and 7.4.3.

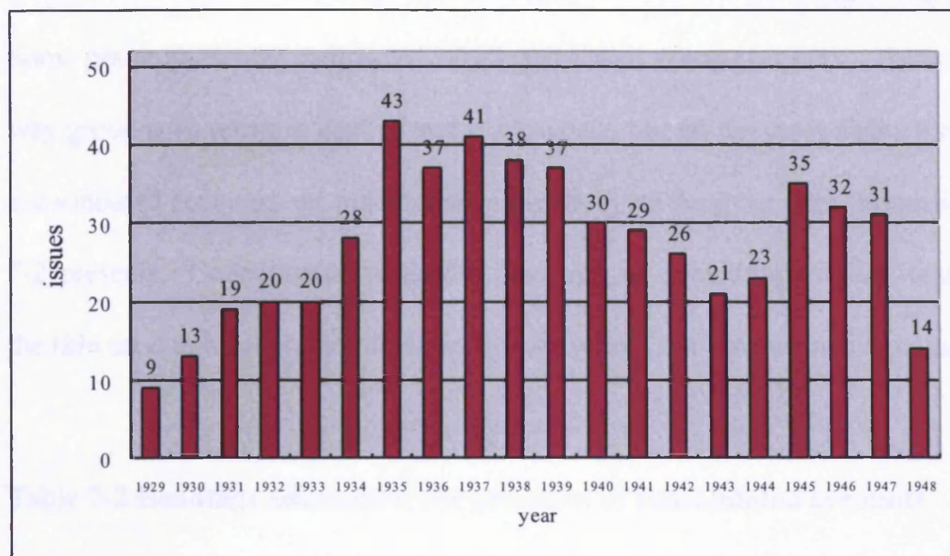
Table 7-1 Frequency of comments on group accounting practices appearing in the Finance & Commerce section

	issues	*issues with group accounts topics*	*per cent*
1929	52	9	17.3%
1930	52	13	25.0%
1931	52	19	36.5%
1932	53	20	37.7%
1933	52	20	38.5%
1934	52	28	53.8%
1935	52	43	82.7%
1936	52	37	71.2%
1937	52	41	78.8%
1938	53	38	71.7%
1939	52	37	71.2%
1940	52	30	57.7%
1941	52	29	55.8%
1942	52	26	50.0%
1943	52	21	40.4%
1944	53	23	43.4%
1945	52	35	67.3%
1946	52	32	61.5%
1947	52	31	59.6%
1948	52	14	26.9%
Total	1,043	546	52.3%

Source: *The Accountant*

76 Such topics as holding company directors' remuneration were excluded from the investigation.

Figure 7-1 Frequency of comments on group accounting practices appearing in the Finance & Commerce section



Source: *The Accountant*

Out of 1,043 weeks between 1929 and 1948, 546 weeks dealt with group accounting issues. In other words, readers of the section were provided with examples of group accounting practices and the accountancy profession's comments on them in every other issue on average throughout the period between 1929 and 1948. The finding suggests that the accountancy profession's attitude exemplified in the Finance and Commerce section of *The Accountant* turned to positive involvement with the group accounting debate at an early stage of the period between 1929 and 1948. The profession, as epitomised by the columns of *The Accountant*, repeatedly dealt with the matter of group accounting throughout the period investigated.

It can also be observed that the years of 1935 (82.7%) and 1945 (67.3%) are each at the top of a trend reflecting an increase in numbers of comments. The years 1943 (40.4%) and 1948 (26.9%) see a tendency towards less comment.

7.4.2 Support for consolidation

The nature of the comments on group accounts varies considerably. Some point to the existence of holding company accounting problems without suggesting possible solutions. Some praise particular companies which published group accounts. Some issues criticise the way group accounting is carried out. However, one of the most distinctive tendencies is that consolidated accounts are put forward repeatedly as the most appropriate solution. As Table 7-2 presents, 'Consolidated Accounts Needed', or something similar, featured repeatedly as the title used to head up the comments made within the Finance and Commerce section.

Table 7-2 Headings advocating the adoption of consolidated accounts

	Date	*Headings*
1	12/12/1931	**Combined Statement Essential**
2	2/1/1932	**Useful Consolidated Balance Sheet**
3	16/1/1932	**Combined Statement Needed**
4	6/2/1932	**Consolidated Accounts Needed**
5	19/5/1934	**Consolidated Accounts Needed**
6	28/11/1936	**Consolidated Accounts Needed**
7	10/7/1937	**Consolidated Accounts Needed**
8	7/8/1937	**Consolidated Profits Needed**
9	1/1/1938	**Consolidated Accounts Needed**
10	25/6/1938	**G.E.C. Consolidation Needed**
11	17/9/1938	**Consolidated Earnings Needed**
12	27/1/1940	**The Importance of Consolidation**
13	17/2/1940	**Consolidated Earnings Needed**
14	13/4/1940	**Importance of Consolidated Earnings**
15	6/7/1940	**Consolidated Account Needed**
16	20/7/1940	**Consolidated Account Needed**
17	3/8/1940	**Consolidation Needed**
18	24/8/1940	**Consolidation Needed**
19	9/11/1940	**Consolidated Statement Needed**
20	12/4/1941	**Consolidated Statement Needed**
21	20/9/1941	**Consolidated Statement Needed**
22	4/10/1941	**Consolidated Statement Needed**
23	25/10/1941	**Consolidated Statement Needed**
24	22/4/1944	**Consolidated Accounts Needed**
25	23/9/1944	**Consolidated Statements Needed**
26	10/3/1945	**Consolidation Desirable**

Source: The Accountant

For illustrative purposes, the following is a typical example of the kinds of comments made under the title 'Consolidated Accounts Needed'.

Consolidated Accounts Needed

A further qualification is added to the auditors' certificate on the balance sheet of The Union Cold Storage Company, Ltd. For seven years running the report has been rendered 'subject to the value of the shareholdings in subsidiary companies' and as we have previously pointed out, the company does not publish consolidated accounts, so that apart from the directors' assurance that there are sufficient undistributed profits in the group to cover losses, shareholders have no further approach to the matter. To this long-standing qualification, the auditors also now make their report subject 'to the adequacy of the reserve referred to in Note 1' and Note 1 on the balance sheet says that 'there are considerable claims for taxation which are not admitted and are under appeal but a substantial reserve is available in provision for contingencies and in the undistributed profits of subsidiary companies for which credit has not been taken in this company's accounts.' A similar note appeared last year, but in that case, the contingencies reserve alone (of unstated amount) was then sufficient to cover the possible liability. In considering these points of uncertainty, it may be noted that assurance is given that the profit of the subsidiaries 'is in excess of the net income (dividends declared, less certain losses partly relative to prior years) from subsidiary companies included in this company's profit and loss account.' The holding company, it may be further noted, is paying 10 per cent. on £1,000,000 of ordinary stock for the 35th consecutive year, the ordinary stock following £11,000,000 of preference capital. *Consolidated accounts, however, are an obvious necessity.*

(*The Accountant*, 10 July 1937: 63, *emphasis added*)

Similarly, when a company adopted consolidated accounts, the journal complimented the company's directors and used admiring headings as shown in Table 7-3.

Table 7-3 Welcoming the adoption of consolidated accounts

	Date	*Headings*
1	23/4/1932	**The Right Spirit**
2	26/8/1933	**In Proper Form**
3	30/12/1933	**Good Intentions**
4	6/1/1934	**In Proper Form**
5	30/6/1934	**A Good Beginning**
6	16/3/1935	**The Right Emphasis**
7	29/8/1936	**The Right Way**
8	5/12/1936	**Brickwood's Good Example**
9	13/2/1937	**A Sound Step**
10	5/6/1937	**A Good Start**
11	23/10/1937	**A Good Example**
12	13/11/1937	**An Excellent Start**
13	2/4/1938	**A Good Start**
14	28/5/1938	**Good Holding Company Accounts**
15	9/7/1938	**Good Practice**
16	25/5/1940	**Very Satisfying**
17	7/9/1940	**Almost a Model**
18	1/2/1941	**A Fine Example**
19	23/5/1942	**A Good Example**
20	3/10/1942	**Satisfying Accounts**
21	2/9/1944	**Satisfactory Accounts**
22	3/2/1945	**A Fine Example**
23	5/1/1946	**A Good Example**
24	26/4/1947	**Excellent Example**
25	3/5/1947	**Excellent Example**

Source: The Accountant

The following is one typical example of the type of comment made.

> **A Good Example**
> We reprint this week the accounts issued recently by Seager, Evans & Co., Ltd., the distillers ... From the accountancy aspect, the main interest is in the form of the accounts, in the provision of a consolidated balance sheet which extends to sub-subsidiaries and in the consolidated profits statement. By this means, the directors have provided the information which is essential in the case of a company holding extensive interests in other businesses under its control ... Minor [further] improvement might be suggested, such as the statement of profits applicable to minority interests as a deduction from the total profits of the group and the continuation of the accounts to show the complete story of the appropriations of profits, but the accounts as they stand are a good example of the information required from a holding company.
>
> (*The Accountant*, 23 October 1937: 573)

Accordingly, for the readers of the journal, consolidated accounts must have appeared a 'right', 'proper', 'good', 'sound', 'fine' and 'excellent' way of financial reporting, all being terms used in the published assessments.

Table 7-4 selects other headings to reveal why the journal considered the publication of consolidated accounts to be the right way forward. These headings used such terms as 'modernity[77]', 'progress', 'forward steps' and 'improvement'. The terms used in Table 7-4 are substantially similar to those in Table 7-3 in that both complimented the publication of consolidated accounts, but it can be assumed that the terms in Table 7-4 are a little stronger in welcoming a practice considered superior to its predecessor than those in Table 7-3. Here, it is worth noting another example of research which demonstrates the rhetoric of language in promoting accounting change (in that case to a Keynesian economic system based on standardized statistical and accounting data) in Japan soon after World War II (Suzuki, 2007). For example, he states as follows:

> The key actors, both in the statistical and accounting reforms, constantly associated the implementation of a new statistical framework to such phraseology as 'accuracy', 'coherence', 'comparability', 'international', and 'standards', which are all characterized as prerequisites for the development of a 'democratic' economic force following the War. Veiled behind this quasi-definitional correctness of language, more substantial discussions and political debates between Keynesians and Marxists were lost in practice. The Keynesian economic thoughts and practices quietly penetrated Japan on the basis of seemingly neutral and democratic accounting. (Suzuki, 2007: 293)

[77] It might be useful to note here that the 'modernity' that the journal was aiming at was explained as follows:

> **The 'Modern Form'**
> A correspondent asks us to explain what we mean when we refer to accounts prepared in the 'modern form'. Such an explanation is not altogether easy in these days when many accountants are giving considerable thought to the subject. Briefly, however, we might describe the 'modern form' as the method of setting out accounts with the object of conveying the information they contain in the clearest manner to the shareholders.

(*The Accountant*, 6 March 1943: 131)

Table 7-4 Signalling the approval of consolidated accounts

	Date	*Headings*
1	2/7/1932	**Progress in Accounting**
2	20/7/1935	**Improved Accounts**
3	4/7/1936	**Metal Box Improvement**
4	15/8/1936	**A Step Forward**
5	24/4/1937	**Warner's Radio Improvement**
6	3/7/1937	**Further Improvement**
7	29/1/1938	**Westinghouse Improvement**
8	9/4/1938	**Years of Progress**
9	3/12/1938	**Room for Improvement**
10	11/2/1939	**Some Improvement**
11	18/2/1939	**Further Progress**
12	18/3/1939	**A Case for Improvement**
13	11/11/1939	**Improvement**
14	24/2/1940	**Further Improvement**
15	1/6/1940	**A Step Forward**
16	8/3/1941	**Modern Accountancy**
17	27/9/1941	**Modernity Preferred**
18	18/10/1941	**Forward Steps**
19	7/11/1942	**Debenhams Step Forward**
20	26/6/1943	**In the Right Direction**
21	24/6/1944	**Moving Forward**
22	5/8/1944	**Boots Adopt Modern Form**
23	3/3/1945	**Moving Forward**
24	14/7/1945	**Moving Forward**
25	26/7/1947	**Great Progress**

Source: The Accountant

The following is a typical example of comments signalling the approval of the adoption of consolidated accounts, in place of an earlier method of group accounting employed (method 3), by a British company under these kinds of headings.

> **Further Improvement**
> Further improvement has been made in the form of the accounts of Thames Grit & Aggregates, Ltd., for the year to 31st March last, which we reprint. The statements showing the net assets and the capital and reserve of the subsidiary companies have been replaced by a full consolidated statement of the assets and liabilities of the company and its subsidiaries and by a consolidated profit and loss account. As the assets of the holding company mainly consist of shares in its subsidiary operating companies, it is obvious that extended accounts are necessary to show the complete view of the state of affairs. ...
> (*The Accountant*, 3 July 1937: 27)

Together, Tables 7-2, 7-3 and 7-4 present 76 examples of headings praising, directly or indirectly, the adoption of consolidated accounts. However, they are only a part of the

congratulatory comments directed at this version of group accounts through the columns of *The Accountant*. The following is one example of numerous other flattering comments which were not included in Tables 7-2, 7-3 and 7-4. The adoption of a consolidated accounts in this case appears to be triggered by the company making a public issue of shares.

> **Morris Motors Consolidation**
> We are glad to note that Morris Motors, Ltd., has, on the admission of the public investor to a share in the equity of the business, issued a consolidated statement of the assets and liabilities of the Morris group of companies. The subsidiary interests are listed in the legal balance sheet which identifies the subsidiary company, the amount of its capital held and the cost of that holding. There is the M.G. Car Co., Ltd., Morris Commercial Cars, Ltd., Morris Industries Exports, Ltd., The Morris-Oxford Press, Ltd., the S.U. Carburetter Co., Ltd., and Wolseley Motors, Ltd. A schedule of subsidiary interests on these lines should form part of the accounts of every holding company. Book value of these shareholdings, including £862,819 due on dividend, current and advance account, is £1,491,872. One of the points made clear by the consolidated statement is that capital reserves exist in the balance sheets of the subsidiary companies totalling £1,672,998, and the report explains that these were accumulated prior to 31st December 1935. In the legal balance sheet, total assets amount to £11,579,882, which in the consolidated account is stepped up to £14,109,430. A feature of the position is the enormous reserve of net liquid assets amounting after providing for the sum required for the ordinary dividend to over £7,000,000. The revenue obtained from the Morris subsidiaries, however, is still confined to the dividends received and receivable. A consolidated earnings statement is needed.
>
> (*The Accountant*, 8 May 1937: 678)

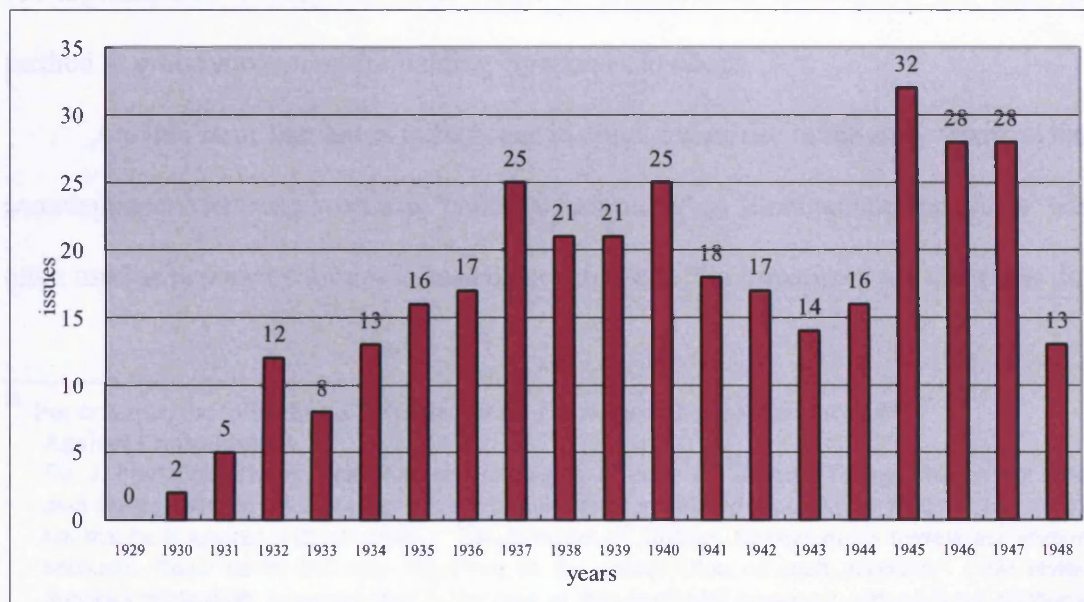
Table 7-5 shows the frequency with which consolidated accounts appeared in the Finance & Commerce section.

Table 7-5 Commenting on consolidated accounts

	issues	*issues with consolidated accounts topics*	*per cent*
1929	52	0	0.0%
1930	52	2	3.8%
1931	52	5	9.6%
1932	53	12	22.6%
1933	52	8	15.4%
1934	52	13	25.0%
1935	52	16	30.8%
1936	52	17	32.7%
1937	52	25	48.1%
1938	53	21	39.6%
1939	52	21	40.4%
1940	52	25	48.1%
1941	52	18	34.6%
1942	52	17	32.7%
1943	52	14	26.9%
1944	53	16	30.2%
1945	52	32	61.5%
1946	52	28	53.8%
1947	52	28	53.8%
1948	52	13	25.0%
Total	1,043	331	31.7%

Source: *The Accountant*

Figure 7-2 Commenting on consolidated accounts*



*This figure will be combined with Figure 7-1 to become Figure 7-3 later below.

Source: *The Accountant*

Table 7-1 identifies 546 (52.3%) issues of *The Accountant* covering group accounts in general as opposed to the 331 (31.7%) in Table 7-5 focusing solely on consolidated accounts.

Almost once in every three issues, on average, the readers were faced with material dealing with the topic of consolidation throughout the period from 1929 to 1948.

It can also be observed that the years of 1937 and 1945 show an increase in numbers of comments. It was in 1935 that comments on group accounting in general increased, while comments on consolidated accounts went upwards in 1937. The years around 1943 see a tendency of less comment. This is the same pattern as Figure 7-1 which depicts the level of commentary on group accounting in general.

It must be noted here that it does not necessarily mean that, in all of the 331 weeks, comments made explicitly advocated the adoption of consolidated accounts. For example, sometimes the contributors of the 'Finance and Commerce' section of *The Accountant* draw attention to the fact that some directors criticize the idea of introducing a requirement for consolidation[78]. In this sense, therefore, the 331 comments are not entirely homogeneous, but together they convey the clear image of consolidated accounts as the most possible method of group accounting for holding companies to adopt.

Another issue that needs to be borne in mind, especially in the early years, is that some commentators used such words as 'combined accounts' or 'amalgamated accounts' which are often used as synonyms for consolidated accounts, but it is sometimes not clear that this is the

[78] For example, the following is the extract from *The Accountant*, 15 February 1947.

Against Consolidation

Sir. J. Frederick Heaton, chairman and managing director of Thomas Tilling Ltd., is not enthusiastic over the prospect of his company having to publish consolidated accounts by force of legislation. It is not that he is against it in principle. The directors of Tillings, he says in his review accompanying the accounts, 'have never had any objection to the presentation of such accounts'. He reiterates his previous contention, however, that in the case of this particular company, consolidated accounts 'might be somewhat misleading and not very helpful'. The fact remains that in a balance sheet totalling £8,111,379, the company shows under the heading of investments in subsidiary companies, £1,998,414 in respect of its holding in Tilling Motor Services Ltd. at par, and £3,600696 for its interests in 'other subsidiary companies at or below cost'. Sir Frederick adds to his words on this subject the statement that 'our interests in the main are in Provincial Omnibus Companies where, although the interests are large, we do not in many cases hold financial control and the figures of these particular companies will not be reflected in the consolidated accounts'. Meantime, we might suggest, it has yet to been seen how far transport nationalisation will proceed. If the full powers sought in the Transport Bill are exercised, passenger as well as goods services will be taken over- and the consolidated accounts controversy will be forgotten. (*The Accountant*, 15 February 1947: 105)

case[79]. These statements may represent the consolidation of the parent's and subsidiary's accounts (method 6), but they might merely represent consolidated accounts of only the subsidiary companies (method 3). It also could be a simple combination of parent and subsidiary company's assets and liabilities (method 4), perhaps even without any elimination of inter-company transactions. Those comments which use 'combined accounts' and 'amalgamated accounts' are not counted in the 331 items summarised in Table 7-5 because of the ambiguity. Also, there are situations where the nature of the extracts remains vague because of the use of descriptions such as[80]:

- 'statement of assets represented by the investments in two other companies' (24 May 1930);
- 'figures were given of the assets, liabilities and profits of the two subsidiaries' (10 January 1931);
- 'a complete statement, not only of the sources of income, but a full review of the finances of the companies from which it is derived' (9 April 1932);
- 'summary of the assets and liabilities of the subsidiaries' (21 July 1934);
- 'statement of subsidiaries' assets' (8 September 1934).

Because of uncertainty concerning the precise significance of these comments, these examples are also excluded from Table 7-5. Therefore, the number 331 is necessarily selective and partial. It therefore provides a probably conservative indication of the frequency (once in every three issues of *The Accountant* throughout twenty years) of comments favourable to the adoption of consolidated accounts. It therefore seems reasonable to conclude that *The Accountant* put forward consolidated accounts repeatedly as the preferred method of group accounting.

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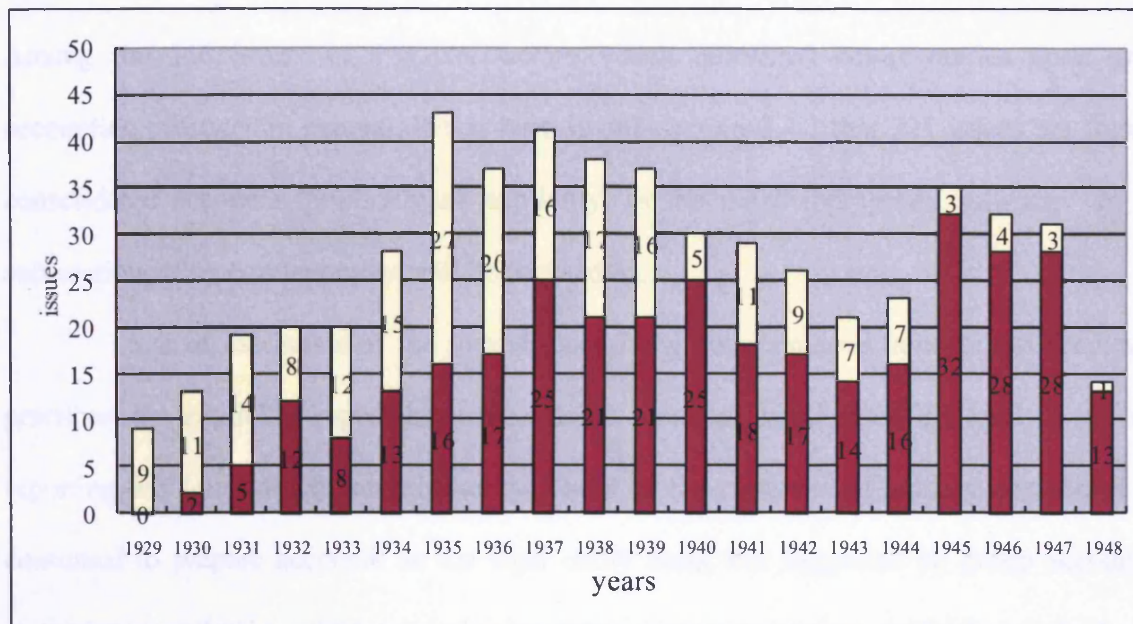
[79] The various terminologies can be found in the comments on 31 September 1931, 26 March 1932, 14 May 1932, 11 June 1932, 5 November 1932, 4 February 1933, 6 May 1933, 27 May 1933, 3 June 1933, 31 March 1934, 28 July 1934, 29 September 1934, 27 June 1936, 21 April 1945 etc.

[80] These examples seem likely to be applications of method 3 or variations thereof.

Figure 7-3 Commentaries on consolidated accounts and other commentaries



Source: *The Accountant*

Figure 7-3 is a combination of Figures 7-1 and 7-2. The lower part of the bars represents numbers of commentaries on consolidated accounts and the upper part represents numbers of other commentaries. It can be seen that the proportion of comments on consolidated accounts has increased throughout the period. Also, it can be found that in 1935 the number of commentaries on group accounting in general increased but that only 37.2% (=16/43) of the commentaries referred to consolidated accounts. On the other hand, in 1937 the number of commentaries upon consolidated accounts increased and the proportion rose to 61.0% (=25/41). The year of 1945 show an increase in the number of commentaries both on group accounting in general and on consolidated accounts (Figures 7-1 & 7-2). Figure 7-3 indicates that the increase of commentaries on group accounting in general in 1945 was due to the increase of commentaries on consolidated accounts. The proportion of commentaries on consolidated accounts rose to 91.4% (=32/34) in 1945.

7.4.3 Other comments

Among the 546 issues of *The Accountant* which contained commentaries upon group accounting practices in general, it was seen in sub-section 7.4.2 that 331 issues put forward consolidated accounts, implicitly or explicitly, as the most appropriate solution. In this sub-section, other commentaries will be focused on.

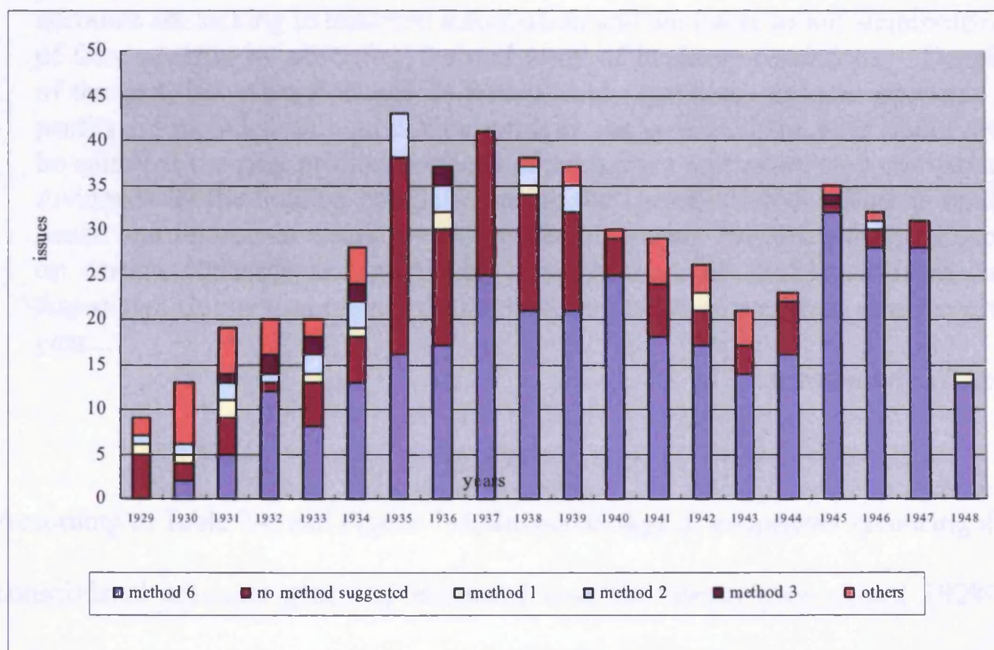
Most of the issues of the journal containing commentaries upon group accounting practices, not explicitly supporting consolidated accounts, highlighted the kind of financial reporting problems which can arise as the result of the existence of holding companies that continued to prepare accounts on the legal entity basis, but suggested no group accounting method as a solution. Commentaries on other group accounting methods (methods 1-5) were seldom found. Table 7-6 and Figure 7-4 show the trends in the level of commentaries on various methods of group accounting.

Table 7-6 Trends in the commentaries on group accounting

	method 6	*no method suggested*	*method 1*	*method 2*	*method 3*	*Others*	*total*
1929	0	5	1	1	0	2	9
1930	2	2	1	1	0	7	13
1931	5	4	2	2	1	5	19
1932	12	1	0	1	2	4	20
1933	8	5	1	2	2	2	20
1934	13	5	1	3	2	4	28
1935	16	22	0	5	0	0	43
1936	17	13	2	3	2	0	37
1937	25	16	0	0	0	0	41
1938	21	13	1	2	0	1	38
1939	21	11	0	3	0	2	37
1940	25	4	0	0	0	1	30
1941	18	6	0	0	0	5	29
1942	17	4	2	0	0	3	26
1943	14	3	0	0	0	4	21
1944	16	6	0	0	0	1	23
1945	32	1	0	0	1	1	35
1946	28	2	0	1	0	1	32
1947	28	3	0	0	0	0	31
1948	13	0	1	0	0	0	14
	331	126	12	24	10	43	546

Source: *The Accountant*

Figure 7-4 Trends in the commentaries on group accounting



Source: *The Accountant*

A typical comment which highlighted the potential financial reporting problems arising from the creation of holding company and subsidiary company relationships, but did not suggest any specific group accounting method as a solution, is reproduced below. It draws attention to two financial reporting problems that arise in the absence of consolidated accounts – the difficulty of establishing the group's true financial position when there are interlocking shareholdings, and the impossibility of assessing true profitability when current year's reported profit includes undisclosed amounts of dividend declared by subsidiaries out of profits earned in earlier years.

> **Confused Profits**
> Two lessons have been thoroughly driven home on the public investor since the war. One is the danger of group finance with interlocking holdings between the companies composing the group – 'financial jerry-building' would be a more appropriate description; the other is the pitfall in company accounts of past profits credited without distinction from the profits of the current period. The disastrous losses of capital that have been associated with these practices should be an absolute deterrent to their continuance. Not that they must lead inevitably to loss of capital; that would be overstating the case. The real reason why no company should issue accounts on these lines – and we are thinking particularly of absence of distinction between past and current profits – is because such accounts are lacking in essential information and are liable to lull shareholders into a sense of false security by obscuring the real trend of business conditions. Despite the lessons of the past, however, Babcock & Wilcox, Ltd., continues to issue accounts in which past profits are included without distinction with the profits of the year under review. It may be said that the past profits are those of subsidiary and associated companies received as dividends by the holding company during the current period. This is made plain in the actual wording of the profit item: 'By Manufacturing Profit for the year including profits on certain contracts not previously brought in, and Dividends from Subsidiary and Associated Companies mainly declared out of profits of previous years received during the year ...'
>
> (*The Accountant*, 27 April 1935: 625)

According to Table 7-6 and Figure 7-4, the percentage of comments favouring the adoption of consolidated accounts generally increased over the twenty-year period 1929-48, while the percentage of comments which provided no suggestion as to any specific group accounting method generally decreased. For example, in 1935, 51.2% (=22/43) of commentaries on

group accounting avoided recommending any corrective method, while in 1945, only 2.9% (=1/35) did so.

As for commentaries upon other group accounting methods, it must be concluded from Table 7-6 and Figure 7-4 that there were a relatively small number of issues that contained comments on them. For example, there were 12 issues that contained commentaries upon the equity method (method 1), but their proportion to all issues discussing group accounting is only 2.2% (=12/546). Compared to group accounting practices where 13% or so of British holding companies adopted the equity method in 1930/31, 1942/43 and 1946/47 (see Table 4-3 of chapter 4), it must be said that the proportion is surprisingly small.

Even though there were relatively few issues that contained commentaries upon the other methods of group accounting, it might be useful to add that such methods are occasionally also referred to favourably in the Finance and Commerce section. Following is an example which is supportive of the equity method though, as stated, only as 'the most useful substitute for a combined balance sheet'.

> **Audited Yield from Subsidiaries**
> The balance sheet of Lever Bros., Ltd. values the holdings in and loans to subsidiary companies at £53,649,860 and shares in allied companies at £7,827,947. In each case classifications are given showing the proportion invested in soap and perfumery, West African products, edible products and land and transport companies. There the information available stops, except for some scraps of information given in the statement required by Section 126 and the auditors' report. In the first-named we are told that the subsidiary companies are treated as branches and the company's proportion of their undistributed profits or losses has been credited to or reserved for in the profit and loss account. So far as it goes this is satisfactory. Even more satisfactory is the statement in the auditors' report that 'the shares in and capital loans to subsidiary companies and the shares in allied companies show an average return of 10.9 per cent. for the year on their total book value.' The inclusion of this calculation in an auditors' report is, we think, unique. It has, however, been a feature in this company since 1927 and is the most useful substitute for a combined balance sheet which we have seen.
>
> (*The Accountant*, 28 April 1934: 605)

Table 7-7 shows the dates when comment on other group accounting methods – the equity method, publishing subsidiary's accounts, and combined statements of subsidiaries (identified as methods 1-3) – appeared in the Finance and Commerce section.

Table 7-7 Comments on use of methods 1-3

	equity method (method 1)	*publishing subsidiary's accounts (method 2)*	*combined statements of subsidiaries (method 3)*
1	13/4/1929	31/8/1929	19/9/1931
2	26/4/1930	2/8/1930	31/3/1934
3	16/5/1931	31/1/1931	29/9/1934
4	21/11/1931	7/2/1931	27/6/1936
5	16/12/1933	4/6/1932	11/6/1932
6	28/4/1934	20/5/1933	5/11/1932
7	22/2/1936	22/7/1933	27/5/1933
8	20/6/1936	7/7/1934	3/6/1933
9	8/10/1938	20/10/1934	30/5/1936
10	10/1/1942	15/12/1934	21/4/1945
11	31/1/1942	23/3/1935	
12	5/15/1948	27/7/1935	
13		10/8/1935	
14		24/8/1935	
15		7/9/1935	
16		11/1/1936	
17		1/2/1936	
18		8/8/1936	
19		26/3/1938	
20		24/12/1938	
21		24/6/1939	
22		16/9/1939	
23		23/9/1939	
24		25/5/1946	

Source: *The Accountant*

7.5 Consistency with previous literature

7.5.1 Influence of Royal Mail case

It was observed (Table 7-1 and Figure 7-1) that the commentators writing for *The Accountant* paid extensive attention to group accounting practices throughout the period from 1929 to 1948. This is strong evidence to suggest that the accountancy profession was quite interested in the matter in those days. As early as 1930, 25.0% (=13/52) of issues contained

comments on group accounting practices in the Finance and Commerce section. In other words, the accountancy profession dealt with the matter as often as once in every four weeks in 1930.

In 1932, the percentage of comments referring to consolidated accounts reveals an early upturn (Table 7-5 and Figure 7-2). The proportion of issues containing comments on consolidated accounts was 15.4% (=2/13) in 1930 and 26.3% (=5/19) in 1931, but it went up to 60.0% (=12/20) in 1932. The year of 1932 immediately follows revelations in the Royal Mail case of 1931 (Brooks, 1933: xxii) and the finding is consistent with the prior assessment of historians, namely that the Royal Mail case encouraged the accountancy profession, here judged to be epitomised by the content of *The Accountant*, to take the initiative in encouraging accounting change[81] (de Paula, 1948: 88; Edwards, 1996: 53; Walker, 1978: 94).

The direct influence of the Royal Mail case on the professional initiatives is stated in Edwards (1976) as follows:

> ... Mr. Justice Wright's charge to the jury, at the Old Bailey on 30 July 1931, incorporated express criticism of the reporting practices of the Royal Mail Company and an implied criticism of the external audit function. These views indicated that the accounting profession might be well advised to devote more effort towards the development and application of higher standards for auditing and reporting financial information. (Edwards, 1976: 298)

The failure of the professional accountancy bodies to take the initiative in issuing guidance for members 'was a disappointment to at least some practising accountants', but with 'the importance of ethical responsibilities emphasised in the professional press, however, there was a voluntary movement towards realism rather than legalism as the basis for financial reports' (Edwards, 1996: 53-4). This chapter shows that the professional press, in the form of the authors of the Finance and Commerce section of *The Accountant* (see for example, Table 7-6) put forward consolidated accounts as the most appropriate group accounting

[81] For example, Walker (1978) argues that 'it seems that the Royal Mail case was a major factor in encouraging the publication of consolidated statements' (Walker, 1978: 94; see also Edwards, 1989a: 232).

method in 1932 in possible response to the views expressed in the Royal Mail case.

7.5.2 Influence of Dunlop Rubber's accounts 1933

In 1935, comments on group accounting in general increased (Figure 7-1). The proportion had risen from 53.8% (=28/52) in 1934 to 82.7% (=43/52) in 1935. The readers of *The Accountant* encountered comments on the matter in 43 weeks of the year. The year of 1935 immediately follows the Dunlop Rubber's consolidated accounts of 1933 (published in 1934). It seems plausible to say that informed opinion within the accountancy profession may have been influenced by these developments. This finding is consistent with previous literature[82]. The following extract from *The Accountant* on the Dunlop accounts gives one example which shows how the profession praised the practice[83]. It justifies extensive quotation.

> **Dunlop's New Standard**
> It is almost impossible to find sufficient praise with which to acclaim the new standard in company accounting set by the 1933 accounts of the Dunlop Rubber Company Limited. Our best commendation is really their appearance in this week's issue of *The Accountant* so that the accountancy profession itself may see the high level of informativeness that is possible in company accounts, particularly in the case of holding companies, if the determination of the management and officials is directed towards that end. These accounts answer all the present-day criticism regarding the obscurity that is possible in the earnings and assets of subsidiary companies when accounts are presented in the manner allowed by law. Especially do they cover those points such as the holding-up of profits in the accounts of subsidiaries and the accumulation of secret reserves and the subsequent declaration of dividends by subsidiaries wholly or partly out of profits of previous years. These points are covered in the Consolidated Statement of Profits, now issued for the first time, in items II and IVe, the narrative of which can be followed in the reprinted accounts and is self-explanatory. These two entries in fact may be regarded as pivotal entries in the Consolidated Statement of Profits as showing profits withheld from distribution by subsidiaries (IVe) and profits received from subsidiaries not applicable to the period of the accounts (item II). ...
>
> (*The Accountant*, 12 May 1934: 676)

[82] For example, Kitchen (1972) describes the Dunlop Rubber's accounts as 'a real step forward in the standard of published group accounts' (Kitchen, 1972: 134).

[83] The commentators of Finance and Commerce section of *The Accountant* repeatedly featured and praised the Dunlop Rubber's accounts; Dunlop's New Standard (12 May 1934); The Dunlop Accounts (4 May 1935); The Dunlop Accounts (16 May 1936); Another Dunlop Innovation (17 April 1937); Years of Progress (9 April 1938); Dunlop Progress (8 April 1939); Dunlop Developments (27 April 1940).

It should be noted here that the Royal Mail case and Dunlop Rubber's 1933 accounts do not appear to have stimulated levels of comment in *The Accountant* at the highest annual levels during the period surveyed.

According to Figure 7-2, the upturn of comments on consolidated accounts in 1932 is not as dramatic as the upturn in 1937 and 1945. In addition, the number of comments favouring consolidated accounts decreased in the next year (1933). Though it can be seen that the Royal Mail case did encourage the publication of consolidated accounts, it must be concluded that the effect was limited.

Similarly, the influence of Dunlop Rubber's practice must perhaps be assessed as relatively modest. It is true that comments on group accounting in general increased in 1935, but comments without any suggested group accounting method also increased in the same year. In 1932, 60% (=12/20) of comments referred to consolidated accounts, but in 1935, 51.2% (=22/43) of comments suggested no method as solution of holding company accounts problems (Table 7-6 and Figure 7-4). These proportions indicate that the opinion-formers within the accountancy profession, at this stage, remained inclined to think that the best group accounting method would be decided, not by them, but by holding company directors and their shareholders. It was not until 1937 that comments referring to consolidated accounts increased again (Table 7-5 and Figure 7-2). In the previous year (in 1936), 45.9% (=17/37) of comments referred to consolidated accounts as the appropriate method for adoption, while there were 61.0% (=25/41) of comments favouring consolidated accounts in 1937. It can be seen in Figure 7-3 that, after this year, the proportion of comments upon consolidated accounts to those upon group accounting in general increased, to 55.3% (=21/38) in 1938, to 56.8% (=21/37) in 1939 (Figure 7-3) and to 83.3% (=25/30) in 1940. The reason for this is not clear, but it can be argued that unceasing compliments up to 1940 on Dunlop Rubber's consolidating practice from the commentators of Finance and Commerce section of *The*

Accountant (see footnote 83) might have had a cumulative effect upon the positive attitudes towards consolidated accounts during this period.

7.5.3 Influence of RoAP7

Between 1941 and 1944, there were fewer numbers of comments on group accounting in general published in the Finance and Commerce section of *The Accountant*. For example, in 1943, 21 issues of *The Accountant* contained comments on the matter of group accounts in the Finance and Commerce section (Table 7-1 and Figure 8-1). The number of 21 is small, especially compared with 1935, when 43 issues of the journal contained comments relating to group accounting. This decrease is likely to have been caused by the wartime conditions of paper in short supply. The journal issues were much shorter during the war years and the number of comments appeared in Finance and Commerce section correspondingly almost halved.

After 1945, there can be observed a clear attitude within the accountancy profession which supported consolidated accounts. For example, 69.6% (=16/23) of comments favoured consolidated accounts in 1944, while the proportion increased to 91.4% (=32/35) in 1945, 87.5% (=28/32) in 1946, 90.3% (=28/31) in 1947 and 92.9% (=13/14) in 1948. The first of these years immediately follows the issue of RoAP7 in 1944, and it seems reasonable to say that the conclusions reached by the leadership of the ICAEW, as reflected in RoAP7, affected the content of *The Accountant*. Zeff (1972: 23) noted that the series of RoAPs proved acceptable to the business community, and also, it seems, to the writers for the Finance and Commerce section of *The Accountant*.

In other words, before RoAP7, the accountancy profession was not inclined to affirm the legislative introduction of any specific method of group accounting. It is true that the comments referring to consolidated accounts gradually increased in number and, especially

after 1937, 50-60% of comments relating to group accounting referred to consolidated accounts. Nevertheless, it is also true that, except for 1940, the proportion of comments on consolidated accounts compared with those on group accounting in general was not overwhelmingly high until the issue of RoAP7. According to Table 7-6, the proportion was 61.0% (=25/41) in 1937, 55.3% (=21/38) in 1938, 56.8% (=21/37) in 1939, 62.1% (=18/29) in 1941, 65.4% (=17/26) in 1942, 66.6% (=14/21) in 1943, and 69.6% (=16/23) in 1944. These proportions seem distinctively lower than 91.4% (=32/35) in 1945, 87.5% (=28/32) in 1946, 90.3% (=28/31) in 1947 and 92.9% (=13/14) in 1948. In addition, as it was mentioned in 7.4.2, not all the comments referring to consolidated accounts simultaneously supported their adoption. Some have merely recorded that there were directors who were not enthusiastic to publish consolidated accounts. In other words, if only those comments which were supportive for consolidated accounts were picked up, the proportion would be much lower in every year. The high proportion of 83.3% (=25/30) in 1940 does not mean that all 83.3% of comments admired the use of consolidated accounts. From these remarks, it is difficult to conclude that the accountancy profession supported extensively consolidated accounts throughout the period. Rather, it seems more reasonable to say that, even though they paid particular attention to consolidated accounts, important opinion-formers within the accountancy profession had not fully determined their attitude, until the issue of RoAP7, concerning their preferred method of group accounting.

7.6 Conclusion

This chapter examined the number and content of comments on group accounting published in the Finance and Commerce section of *The Accountant*. It was found that *The Accountant* had become positively involved with the group accounting debate at an early stage in the

period between 1929 and 1948. Another finding was that, even though consolidated accounts were paid much more attention than any other group accounting method, it was only after RoAP7 was issued that consolidated accounts dominated journal comments on group accounting. The effect of RoAP7 was also seen in the number of comments on group accounting in general, where it increased from 16 in 1944 to 32 in 1945. The effect of the Royal Mail case and Dunlop Rubber's consolidated accounts was observed, but it was noted that the effect was far less evident than that of RoAP7[84].

From these remarks, it is concluded that, despite particular attention to consolidated accounts, important opinion-formers within the accountancy profession had not fully determined their attitude until the issue of RoAP7 concerning their preferred method of group accounting. This attitude between 1929 and 1948 is however shown to be quite different from that of Dicksee and D'Arcy Cooper in 1920s who strongly supported the equity method (chapter 6). As seen in chapter 6, Dicksee and D'Arcy Cooper saw the equity method as the most appropriate practice of holding companies in 1920s, whereas the commentators of *The Accountant* did not make up their mind until the RoAP7 was issued in 1944. In connection with the holding company directors' group accounting practices, it seems possible to say that the hesitating attitude discovered in this chapter could have provided an excuse for company directors to prepare no group accounts and to adhere to the legal entity-based accounts. This point will be dealt with further in chapter 9.

[84] The upturn in interest in consolidated accounts in 1937 remains unexplained and is an appropriate topic for future research.

Chapter 8 The accountancy profession's attitudes 3 – the ICAEW's internal records

8.1 Introduction

This is the last of three chapters which aim at obtaining an understanding of the accountancy profession's attitudes towards group accounting in the UK in the first half of the twentieth century. It examines the ICAEW's internal records in order to understand their leadership's attitude in connection with the RoAP7. The RoAP7 is important, because the preceding chapters of this thesis (chapters 5 & 7) revealed that both holding company directors' practices and the British accountancy profession's attitudes were substantially influenced by the issue of the recommendations. This chapter seeks to understand how the leadership of ICAEW produced the recommendation.

The argument in this chapter is based on newly examined archival material and the content of the previous relevant literature. The following three points will be discussed. First, it will be shown that the content of RoAP7 was deeply influenced by the opinion of de Paula, who had been involved in publishing consolidated accounts at the Dunlop Rubber Company in the previous decade and who advocated adoption of that method in his book. Second, the significance for this part of the study of the ICAEW Memorandum submitted to the Company Law Amendment Committee appointed by the Board of Trade in 1943 (hereafter, Cohen Committee) will be examined. Third, it will be argued that the content of RoAP7 achieved a fusion between two different attitudes, one being de Paula' strong support for the publication of consolidated accounts and the other being the preference expressed in the ICAEW Memorandum for allowing choice between available group accounting methods.

8.2 Accountancy profession and period investigated

It has been revealed that the RoAP7 was remarkably important in the development of group accounting in the UK because it substantially affected both holding companies' group accounting practices (chapter 5) and the accountancy profession's attitudes towards group accounting (chapter 7). This chapter examines the attitude of the leadership of ICAEW towards group accounting in connection with RoAP7 in order to see how RoAP7 emerged.

The accountancy profession's attitudes investigated in this chapter are represented by the leadership of the ICAEW. The ICAEW is said to have played an important role in accounting development in the UK and, especially, it has been widely discussed that the ICAEW's Recommendations on Accounting Principles (RoAPs) had a significant impact on new accounting provisions introduced in CA48. For example, Kitchen (1984: 75) described the impact of RoAP7 as follows: 'the Cohen Committee on Company Law Amendment (1942-43) used Recommendations VI and VII as the main planks of their own recommendations which were to be embodied in the Companies Acts of 1947 and 1948'. Edwards (1996) also recorded the significance of the ICAEW in the development of legislative requirements:

> In framing its recommendations on accounting, which formed the basis for the accounting content of the Companies Act 1948, the CLAC [Company Law Amendment Committee] drew heavily on the ICAEW's submission which was, in turn, founded on the *Recommendations* previously issued. (Edwards, 1996: 55-6)

This chapter focuses on the attitude of the leadership of ICAEW towards group accounting in connection with the RoAP7.

It is noted here that, about a decade before the advent of RoAPs, British accountants of the day 'lined up behind either the Society or the Institute' in deciding how to respond to revelations of unsatisfactory reporting practices in the Royal Mail case (Edwards, 1976:

299)[85]. This chapter deals only with the ICAEW's attitudes towards group accounting because the subsequent role of the Society of Incorporated Accountants and Auditors (SIAA) is recognized as limited by accounting historians (for example, Bircher, 1991: 157-8). In contrast, the influence of the ICAEW is said to be an important topic which needs further research beyond the finding that 'the ICAEW was to play a major role in shaping the nature of the Cohen report and thus the subsequent legislation'[86] (Bircher, 1991: 231).

In order to explore the ICAEW's attitude towards group accounting in connection with RoAP7, this study investigates the period between 1942 and 1944. The reason for starting at 1942 is that the Taxation and Financial Relations Committee (hereafter, T&FR Committee) was set up in that year. The T&FR Committee was the committee responsible for the drafts of RoAPs[87]. The first meeting of the T&FR Committee was in July 1942 (Kitchen and Parker, 1984: 110). It was initially chaired by H. M. Barton (later Sir Harold Barton, and President of the ICAEW, 1944-5) but, by the spring of 1943, de Paula was acting chairman, being elected to the chairmanship on a regular basis on 18 November 1943 (Kitchen and Parker, 1984: 110-11).

The reason for terminating the study in 1944 is that the RoAP7 was issued in the year.

8.3 Source of materials

In order to understand better how RoAP7 emerged, the material investigated in this chapter comprises part of the ICAEW's internal records now stored at Guildhall Library, City of

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[85] It is commented that 'perhaps the main difference was that the Society regarded accounting procedures as being sufficiently developed to justify legislative approval and enforcement whilst the Institute did not' (Edwards, 1976: 299).

[86] Noguchi and Edwards (2004) have subsequently examined, from a corporatist perspective, the fundamental direction of influence between the State and the ICAEW concerning the content of RoAPs issued by the ICAEW.

[87] RoAPs were issued by the Council of the ICAEW between 1942 and 1969. The object of RoAPs was to help ICAEW's own members 'in advising ... as to what is regarded as the best practice' (*The Accountant*, 12 February 1944: 74).

London. Seventeen volumes were investigated (Table 8-1), and they consist mainly of (1) the minutes of meetings of the T&FR Committee and its subcommittees and (2) the minutes of meetings of the Parliamentary & Law Committee (hereafter, P&L Committee) and its reports to the Council. The minutes of meetings of the T&FR Committee were investigated, as indicated above, because it was responsible for drafting RoAPs. The reason for investigating the minutes of meetings of the P&L Committee is because that it was also involved in producing the RoAPs. The procedural channel within the ICAEW through which proposed RoAPs has passed is outlined as follows (Zeff, 1972: 11).

(1) one subcommittee (General Advisory Sub-Committee) of the T&FR Committee formulates a draft memorandum,

(2) each of the (then) 14 District Societies [of the ICAEW] forwards their comments on it,

(3) the T&FR Committee approves the draft,

(4) the key members of P&L Committee at first and the full members of P&L Committee at the next stage decide if it should go forth as a RoAP,

(5) and finally the Council gives authorisation.

The P&L Committee was a key committee within the administrative hierarchy of the ICAEW because it 'included, besides the current President, all five past Presidents remaining on Council as at 29th March 1943' (Noguchi and Edwards, 2004: 70) and 'no other committee had so many past Presidents' (Noguchi and Edwards, 2004: 70). In this sense too, it is relevant to investigate the minutes of meetings of the P&L Committee, because they exemplify the attitude of the ICAEW leadership.

Table 8-1 The ICAEW manuscripts investigated in this study

	Shelfmark	*year*	*title*
1	Ms 28411(12)	1938-1942	Council minute books
2	Ms 28411(13)	1943-1946	Council minute books
3	Ms 28412 (7)	1934-42	Committee Meetings minute books
4	Ms 28412 (8)	1942-49	Committee Meetings minute books
5	Ms 28416(8)	1939-1946	General Purposes Committee minute books
6	Ms 28418(12)	1940-1944	Investigation Committee minute books
7	Ms 28418(13)	1944-1947	Investigation Committee minute books
8	Ms 28420(3)	1929-1945	Parliamentary and Law Committee minute books
9	Ms 28423(1)	1942-1950	Taxation and Financial Relations Committee
10	Ms 28424(1)	1942-1960	Taxation Sub-committee (of the Taxation and Financial Relations Committee
11	Ms 28425	1942	Costings (Government Contracts) Sub-committee minute book
12	Ms 28426(28)	1941-42	Reports of committees
13	Ms 28426(29)	1943-1944	Reports of committees
14	Ms 28428	1942	Co-ordination Committee, Bill Committee and sub-committees minute book
15	Ms 35863(1)	1942-1954	Taxation and Financial Relations Committee
16	Ms 35864	1943	Taxation and Financial Relations Committee
17	Ms 35865(1)	1943-1953	Taxation and Financial Relations Committee

Source: Online Library Catalogue (Guildhall Library), City of London (http://217.169.37.147/TalisPrism/)

8.4 Findings and interpretations

The study of manuscript sources produced the following two findings of relevance to this study. (1) An important change took place in the title of RoAP7 three days after de Paula submitted his personal Memorandum to the Cohen Committee. (2) The drafting of RoAP7 was stopped between October 1943 and January 1944, when the leadership of ICAEW was working on drafting the Memorandum to be submitted to the Cohen Committee. The two findings are presented and interpreted along with previous literature and other relevant materials in 8.4.1 and 8.4.2 respectively. In sub-section 8.4.3, based on the interpretations of two preceding sub-sections, an argument will be introduced that the content of RoAP7 achieved a fusion of the accountancy profession's different attitudes towards group accounting.

8.4.1 Influence of de Paula[88]

The first finding of this chapter is that the title of the draft of RoAP7 was changed soon after de Paula submitted his personal Memorandum to the Cohen Committee. Below, it is argued that the RoAP7 emerged in its final form under the strong influence of de Paula.

On 24 May 1943, the P&L Committee reported to the Council of the ICAEW its decision that 'the "Form of Disclosure of the Results of Subsidiary Companies" should be added to the list of matters for consideration by the General Advisory Sub-Committee of the Taxation and Financial Relations Committee' (Ms 28426/29). The next reference to a RoAP on group accounting was contained in the minutes of a meeting of the General Advisory Sub-Committee of the T&FR Committee, held on 10 June 1943, setting out its future programme which included 'RESERVES AND RESULTS OF SUBSIDIARY COMPANIES (Head VIII)', and recorded the fact that 'Mr. Rees and Mr. de Paula also undertook to produce a first draft which is to be circulated to the Sub-Committee only' (Ms. 35863/1: 12). This decision was reported by P. M. Rees[89], chief accountant of Unilever Ltd, to the T&FR Committee on 24th June 1943 (Ms. 28423/1: 37).

An important event for the purpose of this study took place on 17 September 1943, when the title of RoAP7 was changed.

Through the investigation of the materials contained in the ICAEW archive for the period from May 1943 to February 1944 (when the RoAP7 was issued), it was found that the title of the RoAP7 was often changed. Table 8-2 below shows the changing title of the RoAP7.

[88] According to Kitchen and Parker (1984: 81), among his other achievements, de Paula must be remembered 'as a standard-bearer in the movement for fuller disclosure and greater comprehensibility in financial reporting; as the first non-practising member of the Council of the Institute of Chartered Accountants in England and Wales (ICAEW); as a main progenitor of the ICAEW's important Recommendations on Accounting Principles which began to appear under his Vice-Chairmanship and Chairmanship of the ICAEW's Taxation and Financial Relations Committee early in the 1940s'.

[89] Rees was in the chair of the General Advisory Sub-Committee of the T&FR Committee.

Table 8-2 Changing title of RoAP7

Dates	*meetings*	*titles*
24/5/1943	P&L Committee (MS28426/28)	'Form of Disclosure of the Results of Subsidiary Companies'
10/6/1943	General Advisory Sub-Committee of T&FR Committee (MS35863/1)	'Reserves and Results of Subsidiary Companies'
24/6/1943	T&FR Committee (MS28423/1)	'the Presentation of the Profits of Subsidiary Companies'
22/7/1943	General Advisory Sub-Committee of T&FR Committee (MS35863/1)	'Treatment of the Reserves and Results of Subsidiary Companies in the Accounts of Holding Companies'
17/9/1943	T&FR Committee (MS28423/1)	'Disclosure of the Financial Position and Results of Subsidiary Companies in the Accounts of Holding Companies'
12/2/1944	*The Accountant* (publication of the RoAP7)	same as above

Sources: MS 28423/1, 35863/1, 28426/28.

Unfortunately, the actual drafts of RoAP7 under those titles listed in Table 8-2 were not filed with the minutes and appear no longer to be available.

Among the above title changes, it seems possible that the change made on 17 September 1943 was most important for the development of RoAP7. There are three reasons. First, on 17 September 1943, a meeting of the T&FR Committee was held at 11.00 a.m. and a meeting of the General Advisory Sub-Committee of the T&FR Committee was held at 2.00 p.m. There was no other occasion observed in the examined files when the two meetings were both held on the same day to consider recommendations on group accounts during the period investigated. The minutes of the meeting of the General Advisory Sub-Committee reveal that the title of the draft RoAP had been changed at the meeting of the T&FR Committee earlier in the day. The reason for the change of title was not stated, but 'The draft as finally amended was ordered to be sent forward to the Parliamentary and Law Committee of the Institute' (Ms. 35863/1: 15). Second, the ICAEW's internal documents

studied in this chapter recorded the change of title on 17 September 1943 whereas no earlier record was found drawing attention to changes in title. Third, from the titles listed in Table 8-2, it can be observed that earlier titles refer to 'results', 'reserves and results' and 'profits', whereas the final title refers to '*financial position* and results' (*emphasis added*) of subsidiary companies. It seems that the earlier versions could have focused on results only and did not cover the balance sheet aspects, though the final title did. These facts seem to imply that the change on 17 September 1943 has significant meaning, compared to other changes in title.

Why did an important change in title take place on 17 September 1943?

It is the argument of this chapter that the two meetings held on that day were convened to take account de Paula's opinion concerning group accounting. On 14 September 1943, three days before the meetings of the T&FR Committee and its sub-Committee, de Paula took 'the rather unusual step' (Kitchen and Parker, 1984: 112) of submitting a personal Memorandum of evidence to the Cohen Committee. The meeting of the T&FR Committee on 17 September 1943 was chaired by de Paula himself. It seems reasonable to argue that the two meetings were held to discuss de Paula's Memorandum and, possibly, to harmonise the draft of RoAP7 in accordance with his Memorandum.

de Paula's opinion, which was expressed in the personal Memorandum of evidence to the Cohen Committee, has two significant features for the purpose of this study. First, he supported a specific method of group accounting, i.e. consolidated accounts. Second, he emphasised the importance of publishing not only a consolidated statement of earnings but also a consolidated balance sheet.

As for the first point, his strong conviction that consolidated accounts should be the *only* permitted method of group accounting[90] can be clearly seen from his oral evidence

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[90] It is noted here that de Paula made the acquaintance of Garnsey and Stamp, who both supported consolidated accounts. Kitchen and Parker (1984: 87) stated that 'We may presume that de Paula had been present in October 1925 at a London Members' lunch chaired by Sir Gilbert Garnsey, at which Sir Josiah Stamp had given (in an address reproduced in *The Accountant* of 31 October 1925) what he called an

before the Cohen Committee on 19 May 1944[91]. The Cohen Committee asked de Paula for his opinion about the ICAEW's failure to recommend the introduction of legislation requiring the publication of consolidated accounts (see later in this chapter). de Paula answered as follows:

> You know the Institute give variations –Yes. (de Paula, 1944: Qu. 9904)
>
> First of all, the complete consolidated accounts, secondly, the legal balance sheet with the consolidated accounts of the subsidiaries, in groups if necessary, and thirdly, the legal balance sheet with the subsidiary companies' individual accounts. Would you agree that any of those variations might be satisfactory? – Yes, but I would prefer consolidation, and I see no reason why it should not be the one choice. (de Paula, 1944: Qu. 9905)

As for the second point, his emphasis on the simultaneous publication of a consolidated balance sheet and a consolidated profit and loss statement can be seen in the following extract from his Memorandum.

> In my opinion it is not possible to obtain a true and correct view of the state of the financial affairs and the trend of the results of a group of companies, from an examination of the legal balance sheet and profit and loss accounts of a holding company prepared in accordance with the terms of the present Act ... A reasonably clear view of the financial position and trading results of a group of companies can, in my view, be obtained only by the preparation of a consolidated balance sheet together with a consolidated statement of earnings. (de Paula, 1943: para. 36)
>
> I would therefore recommend that the Act should provide that to the accounts of every holding company there should be attached (a) a consolidated balance sheet and (b) a consolidated statement of earnings. (de Paula, 1943: para. 37)

It can be noted here that a strong focus on the importance of publishing both a consolidated balance sheet and a consolidated profit and loss account was not a subject that had much

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"outsider's reflections" on "Accountants' Problems of Today", in particular on information presented in balance sheets'. It is also relevant that de Paula was deeply influenced by American accounting practices, where consolidation was widely used by holding companies decades before the U.K. (Zeff, 1974: 6)

[91] In connection to his influence in 1940s, two things can be noted here. First, D'Arcy Cooper, who was assigned an important position at the Board of Trade ('Lever Brothers & Unilever' *The Times*, 10 October 1941, reprinted in the annual report and statement of accounts of Lever Brothers & Unilever Limited for the year ended 31 December 1940) and strongly supported the equity method, died in 1941. Secondly, members employed in industry and commerce ('non-practising members') formed the majority of the ICAEW membership and in 1943 de Paula was elected to the Council for the fisrt time as a fellow not in practice (Howitt, 1966: 101-2; Zeff, 1974: 6; Kitchen, 1984: 74).

support during discussions, in various quarters of the accountancy profession, until de Paula raised the issue. Rather, it seems that British accountants were inclined to pay significant attention to publication of a consolidated profit and loss account (for example, see the leading article 'The Institute on Consolidated Accounts', *The Accountant*, 12 February 1944: 70). Indeed, de Paula himself agreed that a consolidated profit and loss account was more important than a consolidated balance sheet.

> There has developed a strong demand for the production of so-called 'consolidated Balance Sheets', which are of great assistance, but in my opinion a consolidated earnings statement is of far greater value and importance. (de Paula, 1948: 62)

> It was owing to the limitations of the legal Profit and Loss Account and the legal Balance Sheet of a holding company that the demand for consolidated statements had been growing with increasing force. To follow this method effectively, however, it was necessary to have first the consolidated earnings of the group, and secondly the financial position of the group. (de Paula, 1948: 89)

Nevertheless, de Paula clearly believed it important to publish a consolidated balance sheet along with a consolidated profit and loss statement.

Given the fact that drafts of RoAP7 have not survived, the contention that de Paula's preferences caused significant change in the content of the draft RoAP7, approved at the two meetings held on 17 September 1943, is of a speculative character. However, the following two features can, it is suggested, *reasonably* be considered the result of de Paula's intervention given his strong support for each of them and the lack of support for consolidated accounts shown by the remainder of the ICAEW leadership, as demonstrated below.

- RoAP7, when issued, clearly favoured consolidated accounts.
- The title was changed to include not only 'results' but also 'financial position' of a holding company group.

This point is consistent with the previous literature. For example, Kitchen and Parker (1984: 81) describe de Paula as 'a main progenitor of the ICAEW's important *Recommendations on Accounting Principles*'. Kitchen and Parker also comment as follows:

> It is interesting to note that the subjects of the Recommendations (nos. VI to X) published between October 1943 and June 1945 followed exactly the list of subjects identified by de Paula in his 1933 Preface to *Principles of Auditing* (except that the Recommendations did not yet deal with forward contracts) ... (Kitchen and Parker, 1984: 111)

8.4.2 Hesitant support for consolidated accounts in the ICAEW Memorandum

The previous sub-section argued that the content of RoAP7 was strongly influenced by the opinion of de Paula, especially from the date of 17 September 1943. On the other hand, the RoAP7 was not issued until 12 February 1944. Why did the ICAEW wait for five months to publish the recommendation? What happened or what did not happen between the September 1943 and February 1944? In this sub-section, it will be argued that, in addition to de Paula's strong influence, the content of RoAP7 was affected by the attitudes towards group accounting as expressed in the ICAEW Memorandum to the Cohen Committee.

At the meeting of the General Advisory Sub-Committee held on 28 October 1943, which was the next meeting after that held on 17 September 1943, the chairman [Rees, of Unilever] reported that 'the existing draft No. VIII[92] on Holding Companies is held up for the moment pending the Council's decision on evidence to be tendered by the Institute on Company Law Amendment' (Ms. 35863/1: 17). The draft was again on the table on 20 January 1944. It was recorded that 'He [Rees] submitted the draft of Recommendation VII on "Disclosure of the Financial Position and Results of Subsidiary Companies in the Accounts of Holding Companies" in the form which is now being considered by the Council through the Parliamentary and Law Committee' (Ms. 28423/1: 45). Within a month of this meeting, the RoAP7 was officially issued and published in *The Accountant*. This finding means that the leadership of ICAEW interrupted the process of drafting RoAP7 between October 1943 and January 1944.

Meanwhile, the ICAEW was drafting the Memorandum to be presented to the Cohen

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92 The recommendation on group accounting was numbered VIII until 18 November 1943 (Ms. 28423/1: 42-3; Ms. 28412/8: 37).

Committee (ICAEW, 1943). The Memorandum was approved by the P&L Committee subject to 'certain amendments to be settled by the Drafting Sub-Committee' on 15 November 1943 (Ms 28420/3: 224). The Memorandum was dated December 1943 (Kitchen and Parker, 1984: 113), and was submitted to the Cohen Committee on 25 February 1944 (Noguchi and Edwards, 2004: 73). It can be said that the Memorandum was approved and dated during the period of inactivity concerning the drafting of RoAP7.

The ICAEW Memorandum was drafted by three members of the Drafting Sub-Committee of the ICAEW Memorandum to be submitted to the Cohen Committee, i.e. Barton, Robson and Rees (Ms 28420/3: 224). Rees was also involved in drafting the RoAP7, as noted above. His influence on the early drafts, prior to de Paula's intervention, appears to have been particularly prominent. At the meeting of the General Advisory Sub-Committee on 20 August 1943 'On the proposal of Mr. de Paula a hearty vote of thanks was passed to Mr. Rees for the services rendered by him in the difficult task of drafting this recommendation' (Ms. 35863/1: 14).

There seems to be no surviving material which records the personal opinions of Barton and Robson during this period (from October 1943 to January 1944), but there is an important previous literature which reveals that Rees' general attitude was one of a lack of enthusiasm for consolidated accounts. Camfferman and Zeff (2003: 187-8) observed Rees' ambivalence towards consolidated accounts as follows:

> Sometime during the preparation of the 1942 report [of Unilever] (which was published in September 1943), the decision had been made to move towards a full set of consolidated financial statements. However, in a lengthy August 1943 memorandum discussing all major changes in the 1942 report, Rees made no mention of consolidated balance sheets. As to the consolidated profit statement, he observed that 'so far as can be foreseen, it embraces such recommendations as have been or will be made by the Institute of Chartered Accountants and covers points which will be suggested by them in their evidence before the Cohen Committee' (Camfferman and Zeff, 2003: 187)

Also, according to Camfferman and Zeff (2003: 188), the 1943 report of Unilever suggest that Rees and fellow executives were still rather reluctant converts, and cautioned readers about the consolidated balance sheet as follows:

> The Consolidated Balance Sheet must be read with certain qualifications in mind. The first of these is that, as the Directors have stated on previous occasions, they consider a submission of a statement which consolidates the balance sheets of a group of companies comprised in a world-wide undertaking, involving the conversion of various currencies into one common currency, may tend to be misleading and the Consolidated Balance Sheets now presented must serve as a general guide and no more to the position of the LIMITED Group as a whole so as to show the main trends in the employment of the Company's resources. (The 1943 Report of Unilever, cited in Camfferman and Zeff, 2003: 188)

Thus, the previous literature reveals that Rees did not enthusiastically support consolidated accounts, and that he was reluctant to publish a consolidated balance sheet. Indeed, Unilever did not publish a consolidated balance sheet until 1943, though a consolidated profit and loss account had been presented since 1934. The previous literature notes that ' ... in August 1943 he may still have expected that the case for consolidated balance sheets would be made less forcefully in Recommendation 7' (Camfferman and Zeff, 2003: 188). In addition, based on the fact that the early drafts of RoAP7 were virtually a work of Rees, it is understandable that the wordings of early titles of RoAP7 were possibly focusing on results only. Therefore, it can be said that Rees was reluctant to recommend a consolidated balance sheet as a single means of presenting group accounting information.

The content of the Memorandum of the ICAEW resembles the above attitude of Rees in the sense that neither were enthusiastic supporters of the publication of consolidated accounts. This finding is consistent with the previous literature that reports that the leadership of the ICAEW was 'less positive in its recommendations in favour of consolidated statements than was de Paula in his Memorandum, or, indeed, than was Recommendation VII itself' (Kitchen and Parker, 1984: 113). The ICAEW's reluctance to support consolidated

accounts, as the single legitimate method of group accounting, is reflected in their Memorandum through their acknowledgement of multiple acceptable methods.

> (1) Balance Sheet Aspect
> The Institute recommends that in addition to the information which may be required to be disclosed in the balance sheet of every company there should, in the case of every holding company, be either annexed to its balance sheet or contained therein such information as, after eliminating inter-company indebtedness and inter-company holdings of share capital, will disclose: –
>
> (a) the aggregate of the reserves (including revenue balances) of the holding company and its subsidiary companies so far as these reserves are attributable to the share capital of the holding company and are available for distribution in dividend by the holding company or could properly be treated as so available if declared in dividend by the subsidiary companies.
>
> (b) the aggregate interest, if any, in the share capital and reserves (including revenue balances) of the subsidiary companies of shareholders other than companies the accounts of which are consolidated.
>
> (c) the aggregate liabilities of the holding company and its subsidiary companies.
>
> (d) the distribution of the aggregate resources of the holding company and its subsidiary companies over the several types of assets belonging to the companies.
>
> (e) the direct or indirect interests of the holding company in subsidiary companies whose accounts are, for stated reasons, not consolidated. ...
>
> (2) Profit and Loss Account Aspect
> The profit and loss account which is required to be prepared by all companies under the provisions of the Act should in the case of a holding company contain or be accompanied by a statement containing (whether by way of consolidated profit and loss account or otherwise) either (a) information as to the profit or loss of the holding company after taking into account its share of the aggregate results of the subsidiary companies, or (b) information as to the profit or loss of the holding company and separate information as to its share of the aggregate results of the subsidiary companies. ... (ICAEW, 1943: Head 10 (D))

The ICAEW nevertheless acknowledged the popularity of consolidated accounts with the following comments.

> In recent year there has been considerable expansion in the use and presentation of consolidated accounts and similar information to supplement the legal accounts of holding companies. There is no doubt that the information so given is of material value in a vast majority of cases. (ICAEW, 1943: Head 10 (C))

However, they immediately added that

> There are more methods than one of presenting information of the kind given by a consolidated balance sheet and the Institute thinks it would be a mistake to insist too rigidly on the adoption of any one method, provided that the information is given. (ICAEW, 1943: Head 10 (C)(1))
>
> The information given in a consolidated profit and loss account should be available in one form or another and whilst the Institute does not think it right to insist on any one form for general application it does think that the disclosure of the results of the group as a whole should be made obligatory in other than wholly exceptional cases. (ICAEW, 1943: Head 10 (C)(2))

From those remarks, it can be said that the ICAEW did accept the usefulness of consolidated accounts in 1943 but that they still hesitated to recommend that consolidated accounts should be the only method of group accounting to receive legislative support. Instead, they were willing to accept variation of group accounting methods, requiring group accounting information of the holding company either annexed to its balance sheet or contained therein. In other words, the finding that the drafting of RoAP7 was stopped from October 1943 to January 1944 seems to be related to hesitation on the part of the ICAEW leadership concerning the best way to resolve the question of whether consolidated accounts should be the only method to be required by legislation.

Given the fact that formal consideration of drafting RoAP7 was stopped between October 1943 and January 1944, and that no record is filed and kept concerning the matter, it is impossible to be perfectly certain about the influence of the ICAEW Memorandum to the Cohen Committee. However, RoAP7 recommended three methods of group accounting, though favoured consolidated accounts as most appropriate, and this acceptance of variation can be a result of hesitating attitudes of the ICAEW leadership towards consolidated accounts.

8.4.3 RoAP7 as a fusion of two different attitudes

The previous two sub-sections attempted to describe how RoAP7 emerged. There were

observed to be two different attitudes which were both influential upon the content of the recommendation. Based on the discussion developed above, this sub-section argues that the RoAP7 achieved a fusion of two different attitudes within the leadership of the accountancy profession.

It was argued that RoAP7 was produced under the combined influence of de Paula and the ICAEW Memorandum. There can be observed two different attitudes towards group accounting, one being the belief of de Paula that consolidated accounts are the only acceptable method of group accounting, and the other being the reluctance of the leadership of ICAEW to recognise consolidated accounts as the best method and, instead, to recognise the acceptability of multiple methods of group accounting.

Below is the actual wording of RoAP7, which seems to have achieved a fusion of the different attitudes of accountancy profession. It described a consolidated balance sheet and a consolidated profit and loss account (method 6 in this study, but referred to in RoAP7 as Method (3) – see below) as 'the most suitable for general application' and other two methods (method 2 and method 3 as defined in this study (Method (1) and Method (2) below) as 'suitable only in special cases'. It can be argued that the RoAP7 satisfied de Paula by giving consolidated accounts the status of 'most suitable' and that the RoAP7 appeased the ICAEW leadership by accepting two other methods.

> With the published accounts, statements should be submitted in the form of a Consolidated Balance Sheet and Consolidated Profit and Loss Account or in such other form as will enable the shareholders to obtain a clear view of the financial position and earnings of the group as a whole. (RoAP7, para.1)
>
> The following are three methods of disclosing this supplemental information. Each has its own value and limitations. The first and second methods are suitable only in special cases.
> *Method (1)*: To submit copies of the accounts of each of the subsidiary undertakings. This method is suitable only where it is desired to focus attention on the financial position and earnings of each component of the group ...
> *Method (2)*: To submit statements of the consolidated assets and liabilities and of the aggregate earnings of the subsidiary undertakings as distinct from those of the holding

company …
Method (3): To submit a Consolidated Balance Sheet and a Consolidated Profit and Loss Account of the holding company and of its subsidiary undertakings treated as one group. This method is the most suitable for general application ... (RoAP7, preface)

The fusion achieved by RoAP7 is presented in Table 8-3.

Table 8-3 A fusion achieved by RoAP7

	de Paula's Memorandum (September 1943)	ICAEW Memorandum (December 1943)	RoAP7 (February 1944)
Consolidated accounts	best method	one suitable method	best method
other methods of group accounting	not accepted	Accepted	accepted

Source: original

The importance of harmonising the content of RoAPs generally with the Memorandum of ICAEW submitted to the Cohen Committee has been revealed in the previous literature. Noguchi and Edwards (2004:81) quote that 'Rees explained the importance of avoiding any conflict between the Recommendations and evidence to be tendered by the Institute to the official Committee on Company Law Amendment'. Also, the characteristic of RoAP7 as a fusion between different attitudes can be said consistent with previous literature. Kitchen and Parker (1984: 113) stated that 'he [de Paula] must have been very satisfied … with Recommendation VII despite its listing three methods of disclosure … because the Recommendation … said of Methods (1) and (2) that "the first and second method are suitable only in special cases" and of Method (3), "This method is the most suitable for general application"'.

It is true that the RoAP7 and the ICAEW Memorandum were not identical in spite of the fact that the drafting of RoAP7 was stopped during the formulation of the ICAEW Memorandum. However, it is also possible to say that the two materials have the same

attitudes in that both accept variations of group accounting, paying a special attention to potential usefulness of consolidated accounts as the best method.

Thus, RoAP7, which achieved a fusion of different opinions of the accountancy profession, was subsequently reflected in the new provisions on group accounting introduced by CA48[93]. Chapters 5 and 7 of this thesis discovered that the clear preference for consolidated accounts expressed in RoAP7 and CA48 led British holding company directors and *The Accountant* to adopt that method.

8.5 Conclusion

This chapter has examined the ICAEW's internal records in order to understand their attitude in connection with the formulation of RoAP7. It was found that the meetings of the T&FR committee and General Advisory Sub-Committee of T&FR Committee, held three days after de Paula presented his personal Memorandum to the Cohen Committee, changed the name of RoAP7 and possibly its content. It was argued that, as a result of de Paula's influence, the degree of support provided for consolidated accounts was strengthened and the simultaneous publication of a consolidated balance sheet and a consolidated profit and loss statement came

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[93] Followings are extracts from the Section 151 of CA48.

151. – (1) Subject to the next following subsection, the group accounts laid before a holding company shall be consolidated accounts comprising –

(a) a consolidated balance sheet dealing with the state of affairs of the company and all the subsidiaries to be dealt with in group accounts;

(b) a consolidated profit and loss account dealing with the profit or loss of the company and those subsidiaries.

(2) If the company's directors are of opinion that it is better for the purpose –

(a) of presenting the same or equivalent information about the state of affairs and profit or loss of the company and those subsidiaries; and

(b) of so presenting it that it may be readily appreciated by the company's members;

the group accounts may be prepared in a form other than that required by the foregoing subsection, and in particular may consist of more than one set of consolidated accounts dealing respectively with the company and one group of subsidiaries and with other groups of subsidiaries or of separate accounts dealing with each of the subsidiaries, or of statements expanding the information about the subsidiaries in the company's own accounts, or any combination of those forms.

(3) The group accounts may be wholly or partly incorporated in the company's own balance sheet and profit and loss account.

to be recommended.

Another finding of this chapter was that the drafting of RoAP7 was stopped between October 1943 and January 1944. Meanwhile, the leadership of the ICAEW were working on the Memorandum which came to be submitted to the Cohen Committee. It has been argued that the content of RoAP7 was influenced by the leadership of the ICAEW as well as de Paula. The leadership of the ICAEW was reluctant to decide that consolidated accounts were the only method of group accounting, and instead they offered multiple methods of group accounting. The influence was considered to be observed in RoAP7's reference to three methods of group accounting though favouring consolidated accounts.

Based on the discussion above, the main argument of this chapter was then presented. It was that RoAP7 had achieved a fusion between the two different attitudes of accountancy profession towards group accounting, by giving consolidated accounts a status of 'most suitable for general application' and by accepting another two methods. In chapter 6, it was revealed that there were two attitudes of the accounting profession in the 1920s, with one suggesting the equity method and the other preferring multiple methods. However, no attempt was observed to unite the two different opinions. The second chapter which deals with the accountancy profession's attitudes, chapter 7, also discovered that on the one hand consolidated accounts were most favoured among several group accounting methods by commentators of *The Accountant*, but on the other hand there were a significant number of comments which had not fully determined their attitude, until the issue of RoAP7, concerning their preferred method of group accounting. In contrast to two other chapters, this chapter revealed a process in which two different attitudes of the accountancy profession came to be united as one opinion.

Chapter 9 Review and Conclusion

9.1 Introduction

Chapters 4-8 present an investigation of British holding companies' group accounting practices (chapters 4 & 5) and the British accountancy profession's attitudes towards group accounting (chapters 6-8). The purpose of this chapter is to review the conclusions presented in those chapters and to provide a possible fundamental answer to the research question: 'Why was the adoption of consolidated accounts slow in the UK?' It will be shown that the continued tendency for British holding company directors to publish legal entity-based accounts, together with the British accountancy profession's attitudes towards group accounting, resulted in the slowness of adoption of consolidated accounts in the UK.

Some topics which are important but not examined fully in this study will be presented for subjects that require further research. These topics include the relationship of group accounting practices and the size, the relationship of capital market and the type of business of British holding companies. The rhetoric of languages in supporting consolidated accounts as a legislative requirement will be also mentioned.

In addition, the limitations of this study, associated with the selection of the unit of analysis on which it focuses, will be noted. Particular attention will be drawn to the influence of famous newspapers and magazines and the influence of the state. The lack of investigation into individual cases, because of the selection of collective attitudes as units of analysis, is also recognised.

9.2 A fundamental reason for slow adoption

From the evidence collected in chapters 4-8, it seems reasonable to conclude that a fundamental reason for slow adoption of consolidated accounts in the UK was the continued

tendency for directors of holding companies to prepare their accounts on the legal entity basis, which is a conclusion consistent with the British accountancy profession's continued support for the equity method in 1920s and their hesitation to decide the 'best' form of group accounts in the 1930s and 1940s. Consistent with the theory of path dependence, the practice of publishing legal entity-based accounts was shared by a large number of holding company directors and thus became institutionalised, obtaining persistency and stability. In the next two sub-sections, the actions of British holding company directors and the British accountancy profession are evaluated, in turn, in light of the theory of path dependence.

9.2.1 Persistent publication of legal entity-based accounts

First, as for British holding company directors' group accounting practices, it was concluded from the investigation into actual published accounts (chapters 4 & 5) that a relatively constant percentage of holding companies throughout the period (1927/28, 1930/31, 1942/43, 1946/47, and 1950/51) adopted the equity method. Specifically, the percentage of holding companies adopting the equity method was 13.6% in 1930/31, 12.7% in 1942/43 and 13.5% in 1946/47 ('method 1' column of Table 4-3 in chapter 4). In addition, it was observed that 100% of holding companies, which employed group accounting and were audited by Cooper Brothers & Co., published accounts using the equity basis of group accounting for the years 1927/28 and 1930/31 (Table 5-4 in chapter 5). Two-third of holding company clients of three accounting firms (Deloitte, Plender, Griffiths & Co., Alfred Tongue & Co. and Thomson McLintock & Co.) in 1930/31, who adopted any form of group accounts, were also using the equity method (Table 5-4 in chapter 5). The same percentage (66.7%) of group accounting adopting holding companies audited by Price, Waterhouse & Co. employed equity accounting in 1942/43 (Table 5-4 in chapter 5). In short, the equity method has been considered a popular and appropriate method of group accounting by a significant number of British

holding company directors from the 1920s until the passage of CA48. This contrasts with subsequent British experience when consolidated accounts became the single means for group accounting.

At the same time, it was observed that most British holding company directors did not arrange for their companies to employ any form of group accounting until the RoAP7 was issued and CA48 came into force. It was revealed that 92.9% of the holding companies studied in chapters 4 and 5 published no group accounts in 1927/28, and 81.4% of them in 1930/31 and 74.9% of them in 1942/43 did the same ('companies not employing group accounting' column of Table 4-3 in chapter 4). Even in 1946/47, which is after the RoAP7 was issued and before CA48 was introduced, 56.0% of selected holding companies in this study prepared no group accounts in their financial reports (same column of Table 4-3 in chapter 4 as above). In other words, a large number of British holding company directors avoided the decision to step into employing group accounts before the CA48 took effect.

What is the implication of the above findings concerning the group accounting practices of British holding companies from the 1920s through to the 1940s? As mentioned in section 5.4 in chapter 5, it seems possible to say that British holding company directors at that time were continuously inclined to prepare their accounts on the legal entity basis. Indeed even where they chose to employ a system of group accounting, equity accounting for long remained the most popular method and, even in 1942/43, as many companies (12.7%) in the sample used method 1 (equity method) as employed method 6 (consolidated accounts). This is of course significant because equity accounting can be seen merely as a modification of legal entity-based accounting rather than as a radically new system of group accounting. It allows companies to publish key information concerning the performance of subsidiaries without departing significantly from the legal entity based financial reporting framework. Moreover, legal entity-based accounts and equity accounting are identical where subsidiaries

incur losses as, applying the concept of prudence, losses were usually recognized under either system. Where there were profits, equity accounting simply anticipates recognition of profits earned but not distributed by subsidiary companies. Indeed, the strong influence of the law upon British accounting practices was focused on by Dickinson (1924: 272) as an important obstacle against the publication of consolidated accounts by holding companies. Also, the viewpoint that the equity method is a modification of legal entity-based accounts is an idea expressed from time to time in the literature, with the prominent US practitioner Maurice E. Peloubet (1955: 31) remarking that 'the British accountants lean much more to the adjustment and amplification of the holding company statements than do their colleagues in the United States'.

Applying these arguments and given the purpose of this thesis – which is to provide an answer to the question: Why was the adoption of consolidated accounts slow in the UK? – it is appropriate to treat companies that use legal entity-based accounts together with those who use equity accounting as a single group. Adding the numbers of 'method 1' column and 'companies not employing group accounting' column of Table 4-3 in chapter 4, 97.1 (=4.2 + 92.9) % of selected holding companies are identified as members of this group in 1927/28. Similarly, 95.0 (=13.6 + 81.4) % in 1930/31, 87.6 (=12.7 + 74.9) % in 1942/43, and 69.5 (=13.5 + 56.0) % in 1946/47 are publishing legal entity-based accounts, with or without adopting the equity method. These high proportions of companies adhering to legal entity-based accounts can be reasonably said to be a dominant feature of group accounting practice in the first half of the twentieth century.

Applying the theory of path dependence, the publication of legal entity-based accounts was observed repeatedly and can be said to have been a commitment shared by a group of people, and thus institutionalised in the realm of British holding company directors' group accounting practices from the 1920s until the introduction of CA48. The theory of path

dependence suggests that an institutionalised behaviour becomes slow to change, and therefore it seems possible to conclude that the adherence of the holding company directors to legal entity-based accounts was a possible answer to the research question. The persistence of institutionalised behaviour is consistent with the finding that the proportion of holding companies preparing accounts on the legal entity basis in 1927/28 (97.1%) declined only gradually as reported in the previous paragraph. Therefore, it seems possible to explain the slow adoption of consolidated accounts by British holding company directors, utilising the theory of path dependence, and such path dependence ensured substantial adherence to legal entity-based accounts despite such famous events as the exposures in the Royal Mail case in 1931 and the publication of Dunlop Rubber Co's consolidated accounts in 1933.

9.2.2 Factors underlying adherence to legal entity-based accounts

Second, turning to the British accountancy profession as defined for the purpose of this study, it was concluded that the equity method was proposed as an appropriate solution to the accounting problems of holding companies in most of the early literature published between 1900 and 1929 (chapter 6). Support for the equity method was documented by influential figures at that time such as A.L. Dickinson, L.R. Dicksee and F. D'Arcy Cooper. This finding and, of course, the reasons why these writers reached that conclusion, seems to provide a plausible explanation for the initial adoption of the equity basis of group accounting by holding company directors. It is true that there were other writers and prominent accountants, such as Garnsey, who wrote textbooks pointing out that there existed a number of suitable group accounting practices, among which was consolidated accounts. However, as Kitchen (1977: 115) noted, Garnsey was relatively young (40-year-old) when the first edition of his book was published, and his association with civil servants and governmental and quasi-governmental institutions 'made him something less than perfectly acceptable' to

the accountancy establishment. The finding of this study that equity accounting was more popular than any other form of group accounting in 1920s (Table 4-3 in chapter 4) also suggests the limited influence of Garnsey's textbook on group accounting practices in the UK.

In addition, it was discovered from the thorough investigation of the contents of the prominent professional accounting journal, *The Accountant*, from 1929 to 1948, that the contributors to its columns did consistently advocate the adoption of group accounting by holding companies, but that they failed to agree upon the 'best' method of group accounting until the RoAP7 was issued (chapter 7). For example, in 1935, 51.2% of commentaries on group accounting which appeared in the Finance and Commerce section of *The Accountant* avoided recommending any method to correct their omission, while in 1945 only 2.9% failed to do so (91.4% of commentaries supported consolidated accounts in that year) (Table 7-6 and Figure 7-4 in chapter 7). This reluctance to decide on the 'best' method of group accounting is consistent with the attitude of the ICAEW's leadership, as reflected in the content of the Memorandum submitted to the Cohen Committee (ICAEW, 1943: Head 10 (C)(1)). As chapter 8 reports, the Memorandum stated that 'there are more methods than one of presenting information of the kind given by a consolidated balance sheet'. The lack of consistent advice from *The Accountant* could have provided an excuse for company directors to prepare no group accounts and to adhere to the legal entity-based accounts. It certainly provided no strong incentive to question path dependent practices.

In short, this study has traced 'the growth and decline in popularity of the equity method of accounting' (Edwards and Webb, 1984: 40) with fuller evidence presented that provides new and deeper insight. It has focused on the adherence of holding company directors to the legal entity-based accounts as well as the accountancy profession's attitudes towards group accounting, and explained the slow adoption of consolidated accounts in the UK by applying the theory of path dependence.

9.3 Further possible research opportunities

In this section, three points will be suggested as important but not developed sufficiently in this study. The first point is the reason for larger companies which were listed on the Official List to be more likely to use group accounts. Second, there could be a reason why the Commercial and Industrial companies were more likely to publish group accounts than those in the Iron, Coal and Steel industry in 1927/28 and 1930/31, while there is no difference between them in 1942/43, 1946/47 and 1950/51. Third, further research is possible and required into the role of rhetoric in the formulation process of RoAP7 and CA48.

First, this study revealed that large companies which were listed on the Official List were more likely to prepare group accounts, but the explanation for this finding was not clearly provided in this study. One possible reason is, as mentioned in sub-section 5.3.1 in chapter 5, that there may have been a greater divorce between management and shareholders and, therefore, more pressure from shareholders in such companies for more information, if seen from the Neoclassicism paradigm. In other words, small/medium sized and provincial holding companies tended to publish no group accounts because pressure from shareholders was less strong than in the case of large companies on the Official List. In this connection, the traditional Alfred Chandler characterization of British industry concerning their structure of corporate governance, i.e. the way in which groups of British companies were financed, seems important. According to him, some, perhaps many, British holding companies were mainly or substantially family-owned company that invested in other companies which were often permitted a fair degree of local control (Chandler, 1990). If that is how some or many British companies were structured in the 1920s and 1930s, one can perhaps see why they continued to favour legal entity-based accounts. They did not see themselves as being in

close control of the activities of subsidiaries and therefore did not see a logic in including their incomes, expenditures, assets and liabilities in a set of consolidated accounts. The characterization of British industry in contrast to the centrally controlled US groups has been subject to criticism and revision, but it remains a respectable thesis and requires further research.

There seem many other opportunities to explain why large companies listed on the Official List were likely to publish group accounts in the first half of the twentieth century. For example, company directors may genuinely have felt that, in the absence of an agreed method, it was best to stick to 'tried and trusted' procedures. In the case of small/medium sized companies which were listed on a provincial market, the reason why they may have preferred to adhere to tried and trusted procedures may have been because they believed that their users (shareholders, lenders, etc.) were close and intimate enough to understand the limitations of existing procedures but not new ones.

Second, further research is possible for another finding of this study that the Commercial and Industrial companies were more likely to adopt group accounts than those in the Iron, Coal and Steel Industry in 1927/28 and 1930/31, while there was no big difference in 1942/43, 1946/47 and 1950/51. This theme will require a combined investigation with historical analysis of the two industries.

The third point concerns rhetoric in promoting accounting change. This study discovered that contributors to the Finance and Commerce section of *The Accountant* repeatedly complimented companies that used consolidated accounts with such words as 'right', 'good', 'sound', 'fine', 'excellent' and 'improvement'. However, this study did not relate the phraseology to regulatory change of group accounting. As mentioned in sub-section 7.4.2, there is a prior literature which focuses on definitional correctness of language in achieving accounting reform. For example, Suzuki (2007: 293) revealed that

such phraseology as 'accuracy', 'coherence', 'comparability', 'international' and 'standards' was associated in Japan soon after World War II with the implementation of the Keynesian economic system based on statistical and accounting data. In this connection, it seems possible, and necessary, to examine the role of rhetoric in the light of the formulation process of RoAP7 and CA48, which accelerated the use of consolidated accounts.

9.4 Limitations of the study

In this section, three areas will be identified as limitations of this study. These are all concerning the selection of units of analysis. As explained in chapters 1 and 2, this study paid attention to the two units of analysis, relying on the previous literature on the development of group accounting in the UK, i.e., British holding company directors' group accounting practices and the accountancy profession's attitudes towards group accounting. The selected units of analysis enabled some important findings to be presented in chapters 4-8. However, at the same time, other units of analysis were neglected in this study, although some previous literature indicates their potential significance.

First, by selecting British holding company's group accounting practices and the accountancy professions' attitudes, this study left aside the influence of more general literature, that is, the effect exerted by famous newspapers and magazines such as *The Times*, *The Economist*, *Fortune* and so forth. The press criticism of the professional bodies' failure to provide help and advice to accountants in 'the front line' is well known in the financial accounting history (Zeff, 1972: 7-8; Edwards, 1989a: 244). As for the matter of group accounts, it is revealed that *The Economist* strongly commented in favour of consolidation and attacked severely those companies who did not provide consolidated accounts (Kitchen, 1972: 124-5). From Lever Brothers, which already adopted the equity method, it is known

that *The Economist* still demanded more disclosure (*The Economist*, 5 April 1924: 733 cited in Kitchen, 1972: 125). The following statement clearly shows the pressure from financial press for consolidation.

> We urge that the publication of consolidated accounts including balance sheet and profit and loss accounts, should be made compulsory. (*The Economist*, 1943a: Part I 14 (c))

For another example, it was in *The Times* that Sir Arthur Whinney, Sir Gilbert Garnsey, F. D'Arcy Cooper and other prominent accountants presented their view on consolidated accounts in May and June 1925 (Kitchen, 1972: 127-9). It seems clear that leading public newspapers and magazines exerted an important influence upon the development of group accounting in the UK but, given the need to apply parameters in order to make this research study a practical proposition in the time available, the full influence of media has not been captured.

Second, this study did not examine the 'influence of the state' (Noguchi & Edwards, 2004: 73). It is known that 'public accountants had been called in to advise government and Parliament since the early nineteenth century, but closer links were undoubtedly forged between professional accountants and central government as a result of the 1914-18 war' (Matthews et al., 1998: 152). According to Noguchi & Edwards (2004), 'the relationship between the state and accountants blossomed during the inter-war period' (Noguchi & Edwards, 2004: 70) and 'a corporatist structure is discernible in the relationship between the ICAEW and the BoT'[94] (Noguchi and Edwards, 2004: 73). The relationship between the state and the ICAEW in the subject area of group accounting is also important, because previous literature has revealed that Josiah Stamp (1880-1941), who is known as one of 'the [Economic Advisory] Council's three most prominent economists' (Howson and Winch, 1977:

[94] There is a substantial literature on corporatism such as Schmitter (1979), Walker and Shackleton (1995) and Williamson (1989).

156) along with Keynes and Henderson, was a keen supporter of consolidated accounting[95]. He publicly complained that 'the science of making consolidated accounts had not advanced far in this country, though it was well known in America' (Stamp, 1925a: 312) and that 'the consolidated balance sheet is familiar enough in America, but is only beginning to be known in this country' (Stamp, 1925b: 686). Moreover, he made actual efforts to ensure the publication of a consolidated balance sheet for Nobel Industries (*The Economist*, 23 September 1922: 515-7). His contribution in promulgating consolidation practice is well-confirmed (Bywater, 1984; Kitchen, 1972). Stamp maintained a close relationship with the government until his death in 1941 (Bywater, 1984). Hence, at the time of RoAP7 and CA48, consolidated accounts were welcomed by the state (especially in the Board of Trade and the Treasury[96]). However, again, this study did not cover the topic fully.

Third, by selecting groups of people (British holding company directors and the British accountancy profession) rather than individual actors as a unit of analysis, this study did not explore detailed circumstances and cause/effect relations. The examination of more than 1,000 company accounts enabled this study to draw conclusions such as the large holding companies are more likely to publish group accounts in 1927/28, 1930/31, 1942/43 and

[95] As a 'statistician and administrator' (Beveridge, 1959: 817), he has been struck by statistical technique in the handling of social data and had a view that its application (which he called 'the quest for truth and the advance of knowledge') would raise the economics of business almost to the status of an exact science (Stamp, 1921: 507). It is natural, therefore, that he saw accountants as 'the trustees of valuable economic data' (Stamp, 1921: 506) and required them to offer 'aggregate statement of accounts' (Stamp, 1925b: 686) for economic use or statistical analysis. He praised *the Economist*'s quarterly summary of industrial and trading results whereas he criticised accountants' 'doubtless inadvertently "dog-in-the-manger" position' (Stamp, 1921: 506). He also offered the following example to accountants.

> I remember that Mr. Joseph Kidger, of Oldham, performed annually a very interesting and useful service in aggregating the results of 100 spinning companies and showing therefrom the trend of profits and dividends the [sic] series extended for a period of over 30 years. (Stamp, 1921: 506)

[96] The Board of Trade and the Treasury seem to have traditionally taken similar action toward auditors. For example, Stacey wrote: It was suggested that 'no person should be qualified for appointment as an auditor for a public company, unless his name is included in a panel of auditors approved by the Board of Trade' (*The Accountant*, 8 April 1944, p.165). This suggestion is similar to the action taken by the Treasury on the recommendation of the Registrar of Friendly Societies in 1920, when only accountants with certain documentary qualifications were placed on the panel of public auditors.' (Stacey, 1954: 232) Also it might be an useful information that Stamp worked both for the Board of Trade and for the Treasury.

1946/47, but the findings do not provide an explanation for why this happened. Company directors' decision to adopt group accounting might well have been associated with many aspects such as their personal conviction, their relationship with other surrounding people, the size and type of their businesses and their financing arrangements. Those characteristics can be discovered only when each case is investigated in detail. Similarly, although this study made the point that the adherence of holding company directors to the legal entity-based accounts was a fundamental reason for the slow adoption of consolidated accounts in the UK, because it was path dependent, it does not explain exactly why each director tended to stick to the legal entity-based accounts for their company. There are some previous writings that studied individual cases of British holding company in connection with their adoption of group accounting (Edwards, 1991; Kitchen, 1972; Camfferman and Zeff, 2003), but further research is possible and needed for other cases.

Given these limitations, it is obvious that this study is necessarily selective and partial and there are many aspects of the developmental process that need further investigation. In this sense, this study is inevitably tentative, and a flexible attitude towards the study as follows is needed.

> In the same way that we have rewritten the past, we expect future historians to rewrite it, adding to our work, possibly overturning our interpretations, and thereby generating more knowledge. (Boyns and Edwards, 2000: 156)

9.5 Conclusion

The contribution of this study is that it has attempted to provide a more fundamental answer to its research question – 'Why was the adoption of consolidated accounts slow in the UK?' – by drawing on the theory of path dependence. It was explained that the adherence of British holding company directors to the legal entity-based accounts, underlying which was the preference of early writers for the equity method and the lack of agreement on the 'best'

method of group accounting in the 1930s and 1940s, can be considered to have been shared and institutionalised, and thus became slow to change.

There have been presented three points that require further research, i.e. (1) why the larger holding companies rather than the other companies which were listed on Official List were more likely to publish group accounts, (2) why Commercial and Industrial companies were more likely to publish group accounts than those in Iron, Coal and Steel industry in 1927/28 and 1930/31, while there is no difference between them in 1942/43, 1946/47 and 1950/51, and (3) how rhetoric stimulated the advent of regulations favouring consolidated accounts. In addition, it was stated that this study is inevitably tentative because of the need to cover more units of analysis. By continuing this study, it is desired to contribute more to the body of accounting history knowledge, which has a tradition of one hundred years embodying many efforts of preceding earnest accounting historians.

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Ms 28412 (7) (8) Committee meetings minute books
Ms 28416 (8) General purposes committee minute books
Ms 28418 (12) (13) Investigation committee minute books
Ms 28420 (3) Parliamentary and law committee minute books
Ms 28423 (1) Taxation and financial relations committee
Ms 28424 (1) Taxation sub-committee (of the Taxation and financial relations committee
Ms 28425 Costings (Government contracts) sub-committee minute book
Ms 28426(28) (29) Reports of committees
Ms 28428 Co-ordination committee, Bill committee and sub-committees minute book
Ms 35863(1) Taxation and financial relations committee
Ms 35864 Taxation and financial relations committee
Ms 35865(1) Taxation and financial relations committee
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